Economic and Banking Performance
in the Twelfth Federal Reserve District

First Glance 12L

Banks Continued to Navigate a Rising Interest Rate Environment

3Q22

December 2, 2022

Federal Reserve Bank
of San Francisco

Key Takeaways

First Glance 12L provides a quarterly look at economic and banking conditions within the Twelfth District.

Economy: District economic conditions cooled since midyear. Job growth remained substantial through October but slowed relative to early-2022. The Districtwide unemployment rate ticked up to 3.9% in October, and by mid-November initial claims for unemployment insurance were materially above pre-pandemic levels. Rising interest rates weighed on District housing market activity, with prices declining since May – particularly in Washington and Idaho – and existing home sales settling at their lowest level since early-2008. One-to-four family permit activity declined sharply amid deteriorating homebuilder sentiment. Commercial real estate transaction counts and price growth slowed in 3Q22. In the industrial and apartment sectors, vacancies persisted at low levels and rents remained strong despite cooling demand for space. But in most District markets, office occupancy and rental rates deteriorated further.

Banking Conditions: Higher interest rates both helped and hurt banks' performance. Yields on loans and securities repriced more quickly than funding costs, lifting median net interest margins and profits quarter-over-quarter. However, quarterly loan growth cooled, likely influenced by seasonal factors, higher financing costs, and an uncertain economic outlook. Problem loan levels remained low despite inflation and interest rate pressures on borrowers. Median on-balance sheet liquidity eased as banks re-deployed funds into loans, but still exceeded pre-pandemic levels. Further increases in long-term interest rates magnified net unrealized losses among bond portfolios, constraining liquidity options and crimping "book" capital. Deposit demand shifted, leading to an uptick in borrowings, especially among Mid-Sized and Large banks.

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A product of SF Fed | Supervision + Credit

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This report is based upon preliminary data from commercial bank Condition & Income (Call) Reports, Uniform Bank Performance Reports (UBPRs) as well as other public sources. Data have been prepared primarily for bank supervisors and bankers. The opinions expressed in this publication are those of the authors. Opinions are intended only for informational purposes, and are not formal opinions of, nor binding on, the Federal Reserve Bank of San Francisco or the Board of Governors of the Federal Reserve System.

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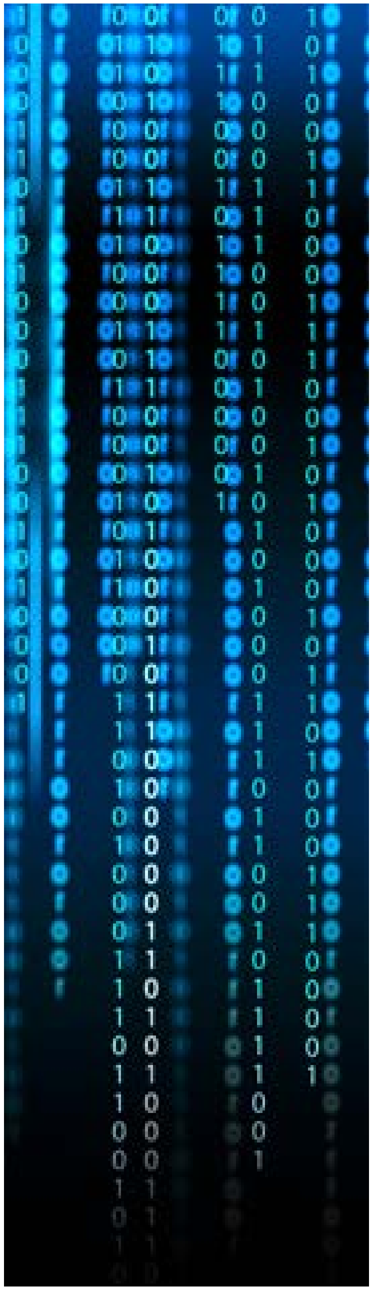
Issues on Our Radar | Selected issues we are watching most closely

Cyberthreats



+ Cyber remains a top risk given an ever-growing multitude of threats, particularly amid evolving geopolitical developments. Ransomware with double extortion, phishing campaigns, patch/vulnerability management, rising cyber insurance premiums, and supply chain compromises are the primary cyber issues facing supervised institutions, their customers, and their suppliers. Hybrid work environments continued to offer opportunities for attacks against virtual private networks and firewall devices.
+ Cyberattacks from nation-state actors have become more frequent, damaging, and widespread with actors targeting infrastructure and the financial services industry. The increase in digital financial services and mobile banking has exponentially expanded the attack surface that criminals can exploit.
+ On October 3, the FFIEC issued an update to the 2018 FFIEC Cybersecurity Resource Guide for Financial Institutions to include ransomware-specific resources to address this increasingly prevalent threat.

Bank Secrecy Act/Anti-Money Laundering (BSA/AML) compliance and fraud

+ BSA/AML monitoring remains heightened because of the District's role in the global economy, the array of activities being conducted by institutions, including cryptoasset-related services, and the evolving nature of threats and regulatory guidance.
+ On October 26, FinCEN renewed and expanded its Geographic Targeting Orders (GTOs) to require U.S. title insurance companies to identify natural persons behind shell companies used in non-financed purchases of residential real estate. GTOs affect several markets in the Twelfth District: Las Vegas, Los Angeles, San Diego, San Francisco, Seattle, Honolulu, and the Hawaiian Islands of Maui, Hawaii, and Kauai.
+ On September 30, FinCEN issued a final rule that establishes a beneficial ownership (BO) information reporting requirement, pursuant to the bipartisan Corporate Transparency Act. The rule will require most corporations, limited liability companies, and other entities created in or registered to do business in the U.S. to report information about their BOs – the persons who ultimately own or control the entity – and in certain cases, their company applicants, to FinCEN. Reporting companies created or registered before the rule's effective date of January 1, 2024, will have one year (until January 1, 2025) to file their initial reports, while those created or registered subsequently will have 30 days after creation or registration to file their initial reports. Both existing and new reporting companies will have to file updates within 30 days of a change in BO information.

Issues on Our Radar | Selected issues we are watching most closely

Real estate loan concentrations

- District banks engage heavily in real estate-related lending, in particular commercial real estate (CRE) mortgages. At 335%, the District's median CRE loan-to-capital and allowances ratio – including owner- and nonowner-occupied NFNR, multifamily, C&LD, and other CRE purpose loans – far surpassed a nationwide median of 198%. Exposures tended to be highest among banks based in California and Washington (see table).
- Rising interest rates may pressure CRE debt serviceability or hurt collateral values if higher financing costs are not offset by a corresponding increase in net operating income. These factors could cause repayment problems, including refinancing risks for balloon payments on maturing CRE loans.
- SFR mortgage concentrations among community banks in the District generally trailed the nation but were above-average among Mid-Sized banks. Higher mortgage interest rates have already slowed new and existing housing markets, which could affect SFR and C&LD lending.

C&I credit risks

- As of 3Q22, District banks' C&I balances represented 60% of tier 1 capital plus allowances on a median basis, comparable to the nation.
- Lingering or renewed stress on business borrowers – from economic slowing, persistent supply chain disruptions, rising input and debt service costs, or labor shortages – may amplify risks inherent in this business line.
- Leveraged loans, which usually carry variable interest rates, posed risks even before the current rate cycle (see Shared National Credit results).

Community bank CECL implementation

- As of 3Q22, more than 80% of District banks – generally smaller, non-publicly traded firms – had yet to adopt CECL. For them, the standard will become effective in 2023.
- The Federal Reserve's CECL Resource Center offers information, including the agency's Scaled CECL Allowance for Losses Estimator (SCALE) and Expected Loss Estimator (ELE) tools for community banks.

Median CRE Loan Concentration
% of tier 1 capital + allowances for loan and lease losses

	Total CRE	NOO CRE
California	365%	266%
Washington	343%	236%
Arizona	306%	204%
Oregon	299%	204%
Nevada	261%	151%
Idaho	250%	170%
Alaska	243%	159%
Hawaii	216%	169%
Utah	167%	88%
Nation	198%	127%

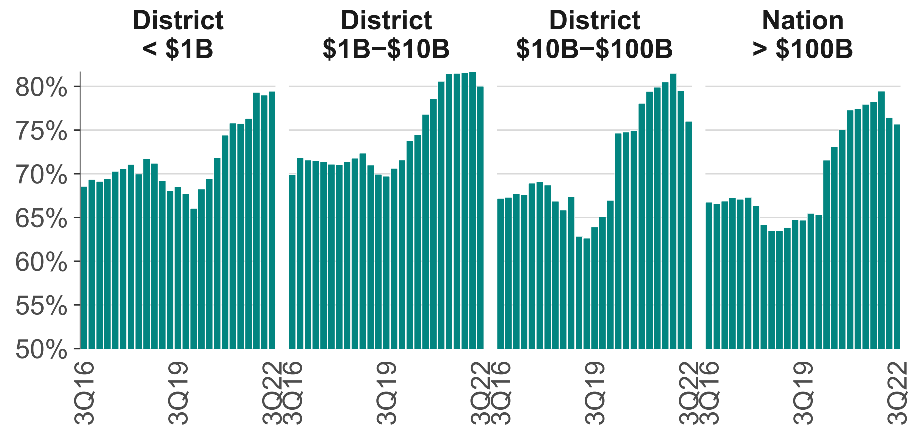
Nonowner-occupied (NOO) excludes owner-occupied nonfarm-nonresidential; Source: Bank Call Reports/UBPRs (September 30, 2022).

Issues on Our Radar | Selected issues we are watching most closely

Funding mix and investment portfolio valuations

+ Annual growth in deposits, particularly low/noninterest-bearing nonmaturity deposits (NMDs) surged in 2020 and 2021, led by flight-to-safety and stimulus-related funding. However, quarterly NMD growth stalled among smaller banks and turned negative among Mid-Sized and Large banks beginning in mid-2022 (see chart).
+ In some cases, pandemic-era NMDs have migrated to higher yielding deposit products and some banks have turned to pricier noncore funding sources to replace runoff. For instance, borrowings increased on a median basis – particularly among Mid-Sized and Large firms – after dipping to historical lows during the pandemic.
+ Rising interest rates continued to erode the fair value of investment portfolios, which largely consist of bonds. As further described on pages 16 and 17, unrealized losses may hamper on-balance sheet liquidity, borrowing capacity, and "book" capital.

Median Nonmaturity Deposits / Total Assets by Bank Size



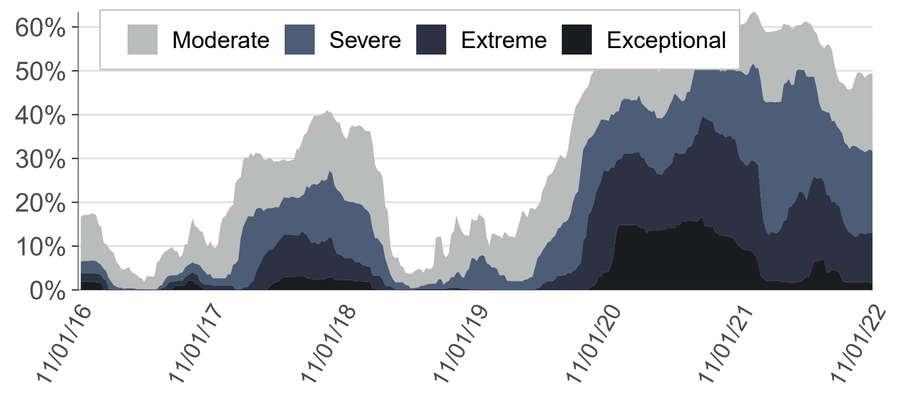
Source: Bank Call Reports/UBPRs.

Drought-related impacts

+ According to the U.S. Drought Monitor, nearly half of the land area in the West Climate Region was in drought through November 1, down from 61% at the same point in 2021 (see chart). Drought remained "extreme" or "exceptional" throughout Central California, Southeast Oregon, and large swaths of Nevada and Utah.
+ Additional water rationing in the Southwest – atop planned cuts to 2023 Colorado River allocations for Arizona and Nevada – seems likely given depleted water levels in Lakes Mead and Powell. On October 28, the U.S. Department of the Interior warned that it may need to take action should negotiations among several states and tribal nations reliant on the Colorado River remain unresolved.
+ Drought threatens water quality and availability, reduces hydropower potential, and contributes to wildfire risks, posing challenges to banks, their employees, and their customers.

Drought Severity, West Region

Percent of land in drought, by severity



West = Twelfth District plus MT and NM. Source: Univ. of Nebraska-Lincoln, U.S. Dept. of Ag., Nat. Oceanic and Atmospheric Admin., 11/1/2022.

Issues on Our Radar | Selected issues we are watching most closely

Increasing enterprise complexity

+ Networks of multiple complex third/fourth party relationships, growing use of cloud services, widening adoption of cryptoasset services, and acquisition of fee-generating businesses are drivers for heightened concern. In particular, bank-fintech partnerships, such as Banking-as-a-Service models, can lead to a growing reliance on nonbank firms for revenue sources and technology firms as service providers. Vulnerabilities can be compounded if the risk appetite for outsourcing and engaging with nonbank partners gets ahead of the control environment.
+ Volatility in cryptocurrency markets continues to highlight operational and financial risks for institutions that engage in cryptoasset activities or provide banking services to crypto-related firms. Federal Reserve SR Letter 22-6: Engagement in Crypto-Asset-Related Activities by Federal Reserve-Supervised Banking Organizations, issued on August 16, indicates that Fed-supervised banks should notify the Fed prior to engaging in cryptoasset activities and that they should implement adequate systems, risk management, and controls in advance of such activity.

Consumer compliance regulatory developments

+ Pending rulemaking includes the Consumer Financial Protection Bureau's (CFPB) Small Business Lending Data Collection proposed rule (published in October 2021, final rule expected March 2023) and the Interagency Community Reinvestment Act (CRA) proposed rule (published in May 2022). An Ask the Regulators webinar, CRA Reform Update: Overview of the Interagency CRA Notice of Proposed Rulemaking – held May 11 but available on replay – provides an overview of the CRA proposal.
+ In January, the CFPB launched an initiative to identify "exploitative junk fees" (see Docket ID CFPB-2022-0003), which resulted in guidance covering debt collection "pay-to-pay" fees as well as assessments on unanticipated overdrafts and returned deposited items.

LIBOR transition

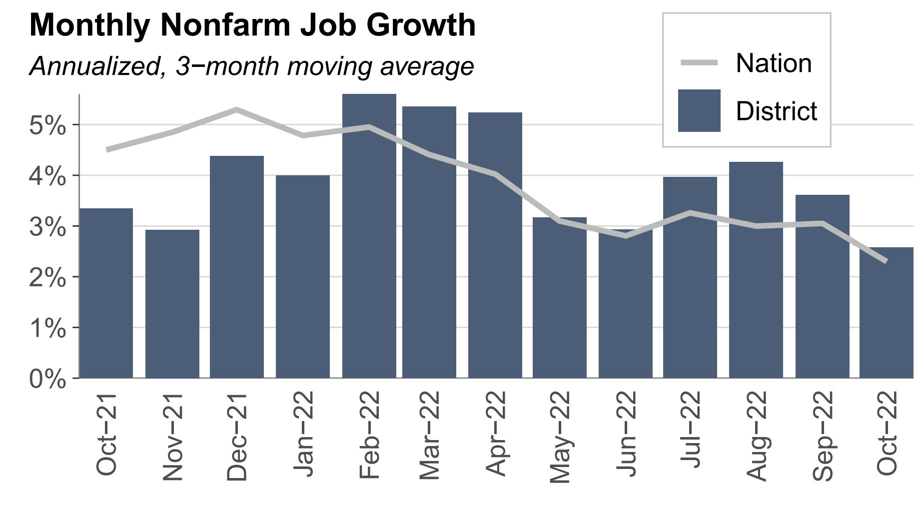
+ LIBOR transition will remain an area of focus ahead of the mid-2023 sunset of LIBOR. The Federal Reserve's LIBOR Transition website provides guidance on instruments with tenors beyond June 2023, which may require renegotiation, fallback language, and/or an alternative reference rate.
+ In July, the Federal Reserve issued proposed rules outlining which Secured Overnight Financing Rate (SOFR)-based replacement rate and spreads would apply to legacy contracts that lack a clearly-defined or practicable replacement benchmark rate (issued pursuant to the LIBOR Act, passed in March 2022).
+ Exposure is generally low among most District banks, primarily via securities, derivatives, and/or subordinated debt. LIBOR-based lending is limited.

For more information: supervisory and financial stability issues related to these and other topics are explored in the Federal Reserve's semi-annual reports on Supervision and Regulation and Financial Stability.

Twelfth District Economy | Employment

Job growth remained robust across District states, but slowed relative to early-2022.

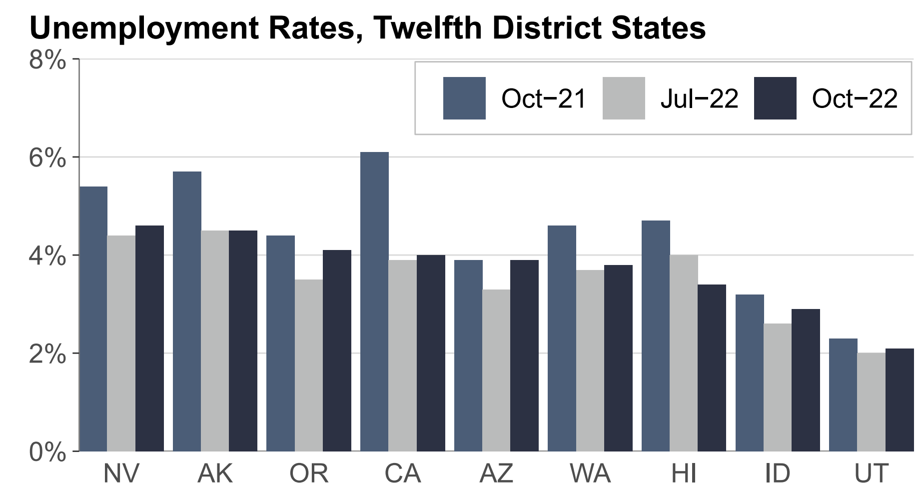
- Total nonfarm payrolls in the District surpassed their pre-pandemic (Feb. 2020) peak in July 2022. Monthly job growth has slowed relative to early-2022, but it remained at a robust 2.6% in October (on an annualized, three-month moving average basis; see chart).
- From August to October 2022, the education/health sector accounted for the largest share of hiring, followed by the leisure/hospitality and professional/business services sectors. On the other hand, hiring in the information (including technology), manufacturing, and government sectors slowed relative to 2Q22.
- By October, Hawaii and Alaska were the only District states where payrolls remained below pre-pandemic peaks, but these states also posted the fastest pace of job growth in recent months, followed by Washington. Job gains in other District states, particularly Arizona and Nevada, have slowed since mid-year.



Seasonally adjusted. Source: Bureau of Labor Statistics.

Unemployment rates edged up recently across the District, and initial unemployment claims increased in November.

- The Districtwide unemployment rate averaged 3.7% in 3Q22 but ticked up to 3.9% in October, slightly below the 4.0% rate just prior to the pandemic (Feb. 2020). However, labor-force participation in the District also stopped increasing during 3Q22, settling at about half a percentage point below the pre-pandemic rate.
- At the state level, unemployment rates increased in all District states except Hawaii from July to October 2022, led by Arizona and Oregon (see chart). Nevertheless, October unemployment rates compared favorably to pre-pandemic rates in all District states except Hawaii, Nevada, and Oregon.
- More recently, initial claims for unemployment insurance in the District increased, to a 3-week average of 70k by mid-November 2022 – meaningfully above the 60-63k range typical of the months preceding the pandemic (late-2019 and early-2020).



Seasonally adjusted. Source: Bureau of Labor Statistics.

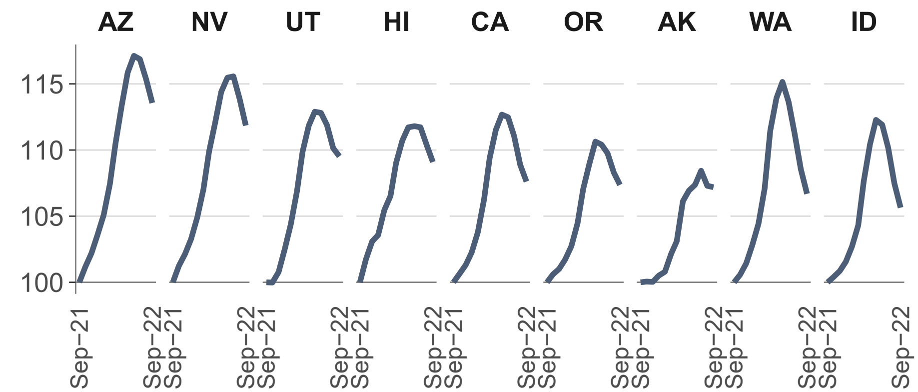
Twelfth District Economy | Housing

District home prices peaked in May 2022; Washington and Idaho saw the largest subsequent price declines.

+ Average single-family home prices in the District peaked in May 2022 and subsequently declined by 4.3% through September. Nevertheless, District home prices were still 8.4% above year-ago levels in September. In comparison, national home prices peaked in June and then fell by 2.0% through September.
+ Home prices declined in all District states from mid-2022 to September, led by Washington (-7.3%), Idaho (-5.9%) and California (-4.5%). As for the District overall, this recent decline in state-level prices only offset part of the run-up since Sept. 2021 (see chart).
+ The recent decline in home prices was not enough to offset the effects of rising mortgage rates and the large pandemic era run-up in prices on housing affordability. Affordability metrics continued to deteriorate rapidly across all District states in 3Q22, particularly in Utah and Nevada.

Home Price Index, Twelfth District States

Sep−21 = 100



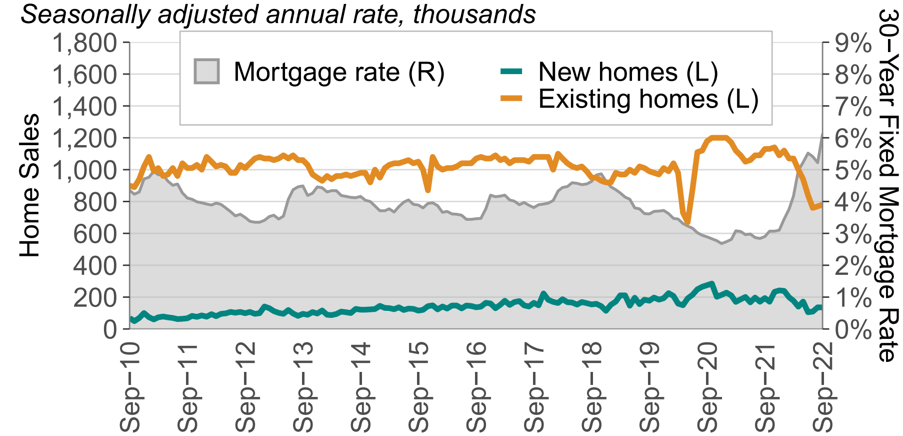
Index covers attached and detached single-family homes, including distressed sales. Source: CoreLogic.

Home sales stabilized in 3Q22 after a sharp drop earlier in 2022, but for-sale inventories increased relative to sales.

+ New and existing single-family home sales in the West stabilized in 3Q22 after falling rapidly earlier in 2022 (see chart). Nevertheless, existing-home sales remained stuck at their lowest level since early-2008, excepting the brief plunge at the start of the pandemic.
+ Additionally, October pending home sales, which typically lead existing sales by 1-2 months, were down 46% from year-ago levels in the West, according to the National Association of REALTORS®.
+ Per Redfin, the pace of new residential listings in the District has declined substantially since June 2022, but due to a combination of falling sales and a large increase in listings through mid-2022, for-sale inventories in the District rose to an average of 2.8 months' worth of sales for the August-October period. This eclipsed the comparable average of 2.6 months' worth of sales in October 2019.

Single−Family Home Sales, West Region

Seasonally adjusted annual rate, thousands



West = District plus CO, MT, NM, and WY. Sources: National Association of REALTORS® (© 2022, reprinted with permission), Census Bureau, Freddie Mac.

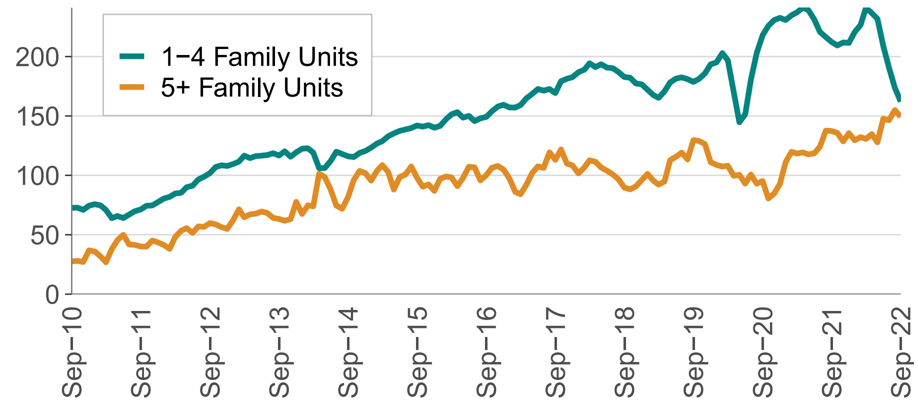
Twelfth District Economy | Housing + Commercial Real Estate

Multifamily permit issuance increased despite falling 1-4 family activity and declining homebuilder confidence.

+ 1-4 family housing permits issued in the District continued to decline rapidly, reaching their lowest level since early-2017 by September, except for the early-pandemic slump (see chart).
+ On the other hand, 5+ family permits issued in the District reached levels not seen since before the Global Financial Crisis, as high mortgage rates forced potential buyers to continue renting and nominal rents kept pace with inflation.
+ Single-family homebuilder confidence in the West continued to decline sharply into 4Q22. By October-November, the NAHB/Wells Fargo Housing Market Index reached its lowest level since early-2012. Builders noted scarce buyer traffic for new homes and continued increases in building costs amid moderating sales prices. Multifamily builder confidence also eased in 3Q22 despite strong permitting, pointing to a potential easing of activity going forward.

Housing Permits, Twelfth District

Seasonally adjusted annual rate, 3−month avg., thousands



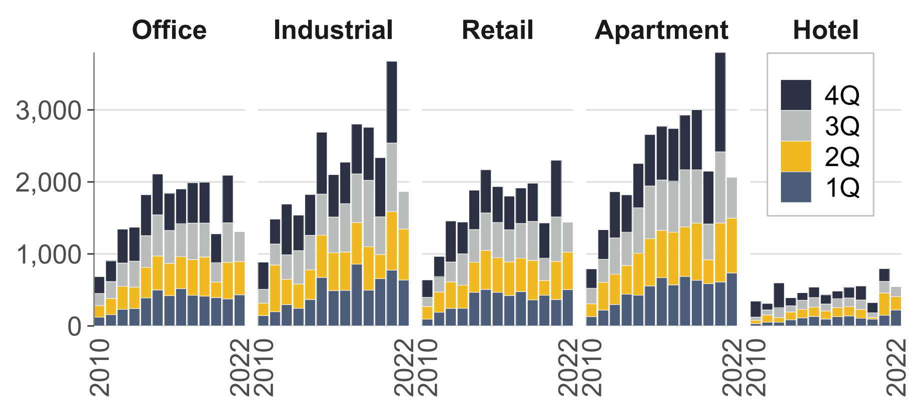
Source: Census Bureau via Haver Analytics.

West-region CRE transactions slowed in 3Q22, falling behind the 2019 YTD pace in most sectors.

+ The pace of CRE transactions in the West slowed further in 3Q22, falling below the 2019 YTD pace for all major sectors except hotel (see chart). This likely reflects both a normalization after the record year in 2021 as well as the effects of higher financing costs.
+ The industrial and apartment sectors saw the largest declines in sales transactions relative to a year earlier, as these sectors also experienced the largest surge in transactions in 2021. Office and retail property sales declined more moderately year-over-year.
+ Per Real Capital Analytics (RCA), the dollar volume of CRE transactions at the national level declined on a year-over-year basis for the third straight month in October 2022. This decline was spread across all sectors except hotel, which was boosted by a large multi-property deal. RCA noted that a gap in price expectations between buyers and sellers likely inhibited dealmaking in recent months.

CRE Transactions, West Region

Number of properties sold



Includes transactions of properties valued $2.5 million and above; West = District plus CO, MT, NM, and WY. Source: Real Capital Analytics.

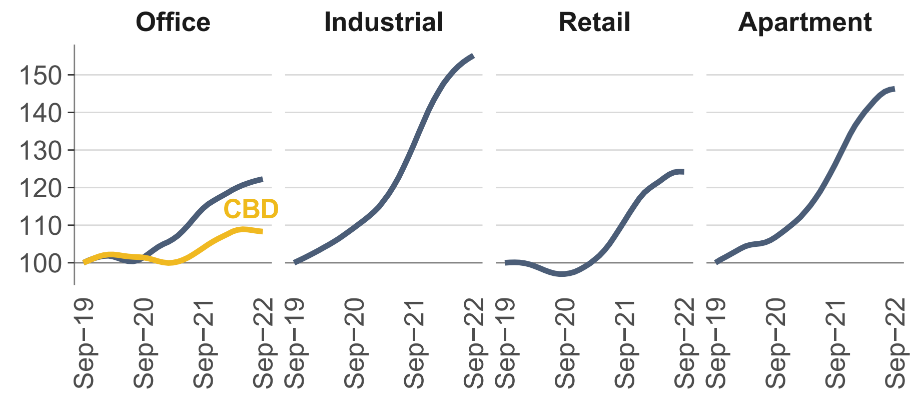
Twelfth District Economy | Commercial Real Estate

CRE price growth slowed across sectors in 3Q22 and turned negative for downtown offices and retail properties.

+ National CRE price growth eased across sectors in 3Q22 (see chart). Downtown (CBD) office prices peaked in June 2020 and declined in each subsequent month through September, although suburban office prices continued to increase, albeit more slowly. Retail property prices also declined slightly in September.
+ Industrial and apartment prices also slowed after standout growth during the pandemic, but the slowdown was more dramatic for apartment prices – they increased by just 1.8% on the month in September (annualized), compared to 6.5% for industrial prices.
+ CRE cap rates in the West continued to decline across sectors, except for a minor uptick for industrial properties. With rising interest rates, the spreads of cap rates to 10-year Treasury rates narrowed further, falling below pre-pandemic lows for the industrial and apartment sectors.

Commercial Property Price Indices, Nation

Sep−19 = 100



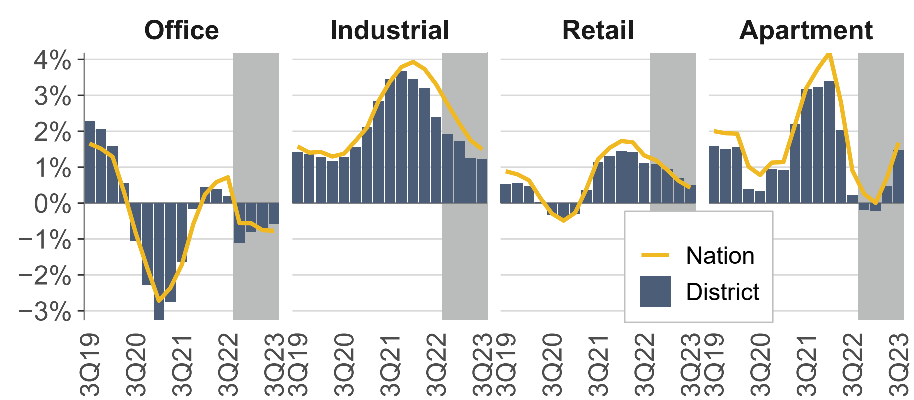
Based upon repeat-sales transactions; CBD = central business district.
Source: Real Capital Analytics.

Demand for CRE space declined across sectors in 3Q22, notably in the apartment and office sectors.

+ The decline in absorption was particularly fast in the apartment sector (see chart), likely due to the exhaustion of the pent-up demand that boosted absorption and fueled the recovery of apartment rents starting in mid-2021. Looking ahead, CBRE-EA expects a lull in apartment demand through mid-2023 followed by a return to growth. Among District markets, Las Vegas, Honolulu, and Tucson had the lowest 3Q22 apartment absorption rates.
+ The office sector, on the other hand, saw only a minor recovery in demand earlier in 2022, and then District absorption declined in 3Q22 despite a modest increase at the national level. CBRE-EA forecasts a return to negative office absorption in 4Q22 as the ongoing remote-work trend combines with weaker economic conditions.
+ Industrial and retail absorption rates remained well above pre-pandemic trends through 3Q22 but may slow prospectively.

CRE Absorption Rates

Rolling 4−quarter absorption as % of ending stock, shaded area = forecast



Includes the 16 to 18 largest markets in the District, depending on the sector.
Source: CBRE-EA, SF Fed calculations.

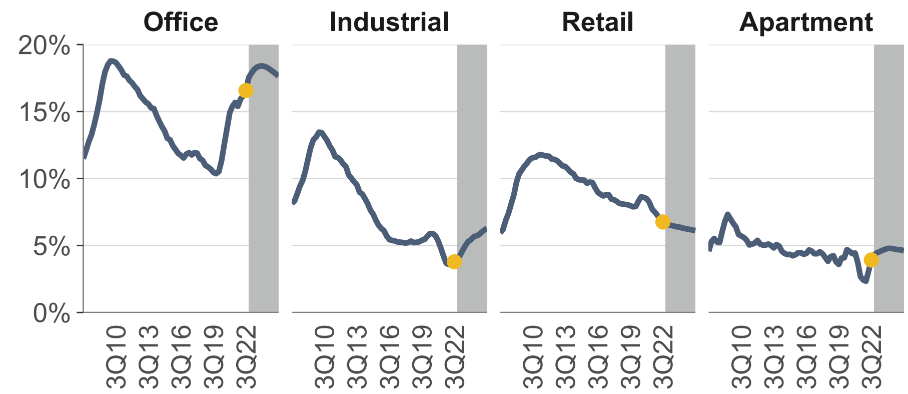
Twelfth District Economy | Commercial Real Estate

Districtwide office vacancies increased, but remained below the national average vacancy rate.

+ Aggregate office vacancies across District markets rose in 3Q22 but remained below their peak during the Great Recession (see chart). The Districtwide office vacancy rate also remained below the national rate, which surpassed its Great Recession peak in 3Q22. Nevertheless, CBRE-EA expects vacancies to rise further amid weakening demand. San Francisco, Salt Lake City, and Portland registered the largest increase in office vacancy rates in the District, relative to 4Q19.
+ Apartment vacancies in the District continued to rise from the historical low reached in 1Q22, approaching levels typical of the quarters preceding the pandemic.
+ The average industrial vacancy rate in the District has been stable at historically low levels since 1Q22, while retail vacancies continued to edge down through 3Q22.

Avg. CRE Vacancy Rates, Twelfth District Markets

Weighted by stock, shaded area = 3−year forecast



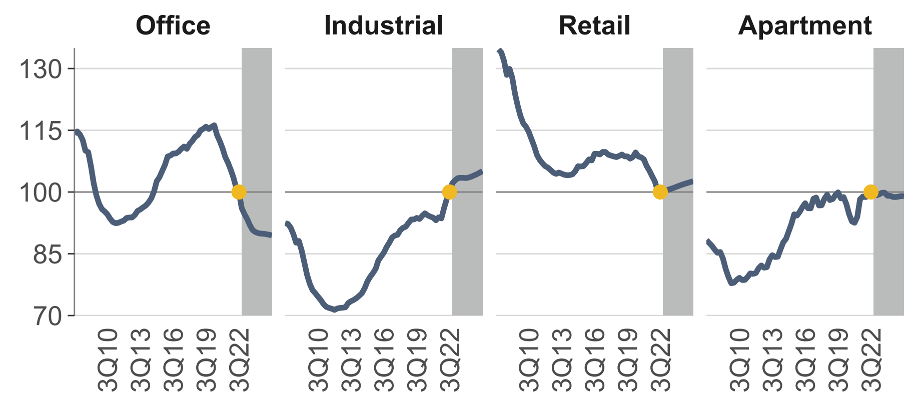
Includes the 16 to 18 largest markets in the District, depending on the sector.
Sources: CBRE-EA, SF Fed calculations.

Office rents declined further while industrial rents reached new highs and apartment rents stabilized.

+ By 3Q22, average real apartment rents in the District fully recovered from the brief pandemic pullback, slightly surpassing the pre-pandemic peak, although rent increases slowed in recent quarters (see chart). Looking ahead, cooling demand (discussed above) will likely keep apartment rents flat in the coming quarters.
+ Real industrial rents in the District continued to rise to fresh multi-decade highs and CBRE-EA has forecasted further increases.
+ The decline in real office rents in the District showed no signs of abating in 3Q22. Real retail rents also continued to fall, but CBRE-EA expects low vacancies and muted supply to support retail rents in the coming quarters.
+ San Francisco remained a notable outlier among District markets for its large declines in real rents since 4Q19 across the office, apartment, and industrial sectors.

CRE Real Rent Indices, Twelfth District Markets

Weighted by stock, shaded area = 3−year forecast, 3Q22 = 100



Asking rents for office and industrial, effective rents for retail and apartment; 16 to 18 largest markets in the District. Sources: CBRE-EA, SF Fed calculations.

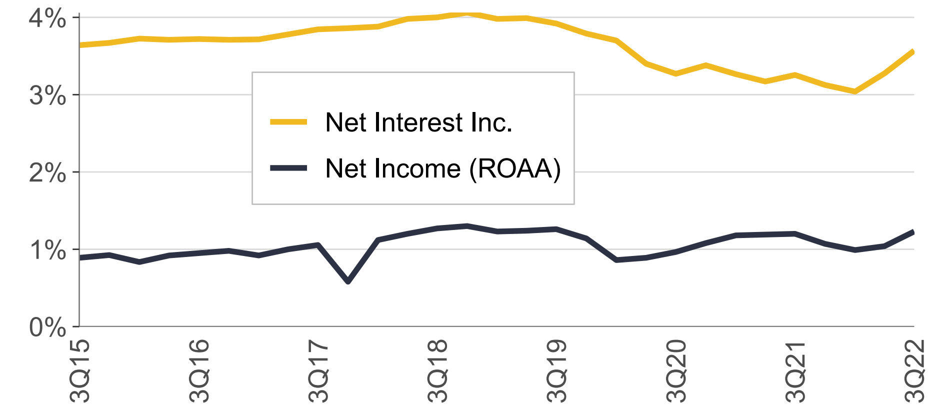
Twelfth District Banking Conditions | Earnings

Earnings performance and profit expectations improved.

- During 3Q22, District banks reported a median quarterly ROAA (adjusted for Subchapter S effects) of 1.23%, up 19 bps from the prior quarter and 3 bps from the year-ago quarter, led by stronger net interest income performance (see chart).
- District banks' median YTD adjusted ROAA also edged up from mid-2022, but underperformed the first nine months of 2021, which had benefited from PPP fee income and reserve releases.
- According to the 3Q22 CSBS Community Bank Sentiment Survey, two thirds of community bankers in the "West," felt profits would strengthen in the coming year, up from half of respondents last quarter, likely reflecting positive net interest margin trends. Bankers anticipating profit growth were also more likely to expect stable or improving future business conditions. Those expecting stable-to-declining profits were often less sanguine about business prospects.

Median Net Interest Income & ROAA, Twelfth District

% of avg. assets, 1−quarter annualized



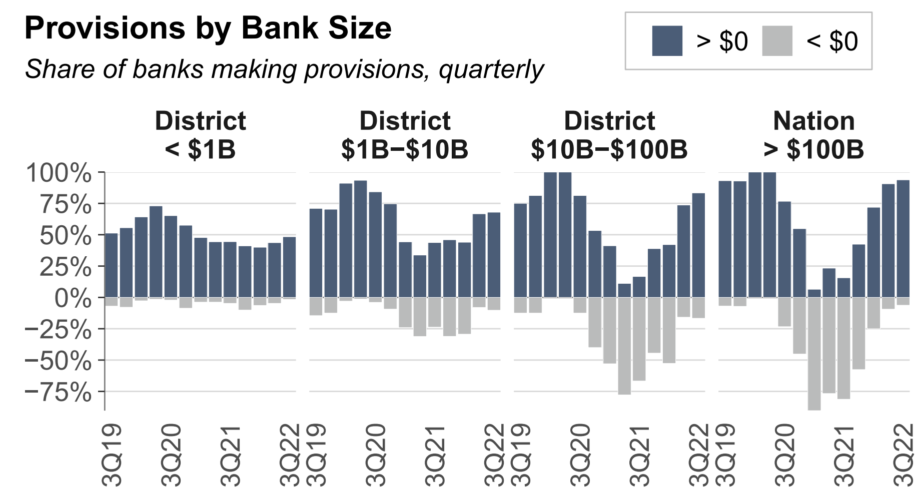
ROAAs among Subchapter-S filing banks are shown net of theoretical tax expense. Source: Bank Call Reports/UBPRs.

Quarterly net interest margins widened significantly; provisioning picked up slightly.

- The median one-quarter net interest income-to-average assets ratio among District banks improved to 3.57% in 3Q22, up 30 bps from 2Q22. Median yields received on earning assets responded more quickly to interest rate increases than funding costs. The trend was fueled by high exposures to variable rate loans and heavy reliance on less rate-sensitive transaction accounts for funding.
- Margin expansion was offset slightly by a 3 bps increase in median overhead and a 2 bps slip in median noninterest income ratios.
- The share of banks incurring quarterly provisions in response to loan growth and/or slower economic prospects edged higher, most notably among Mid-Sized banks (see chart). Overall, 59% of District banks booked positive provisions for loan losses in 3Q22, up from 55% in the prior quarter. Districtwide, 6% of banks released reserves, similar to last quarter, but down substantially from 18% in 3Q21.

Provisions by Bank Size

Share of banks making provisions, quarterly



Source: Bank Call Reports/UBPRs.

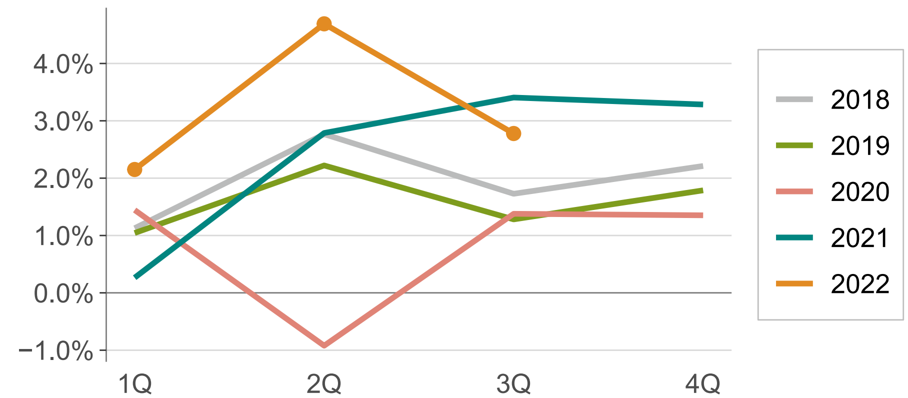
Twelfth District Banking Conditions | Growth + Concentrations

Quarterly loan and lease growth slowed.

+ District banks' median annual non-PPP loan growth rate was strong but decelerated to 14.6%. Likewise, the median one-quarter growth rate for non-PPP loans slowed to 2.8%, likely influenced in part by seasonality (see chart). Based on results of the Fed's October Senior Loan Officer Opinion Survey and IntraFi Network's 3Q22 banker survey, weakening loan demand may have also played a role.
+ Year-over-year loan growth was led primarily by CRE originations, with C&LD, MF, and NFNR balances each expanding at double-digit paces on a median basis. SFR mortgages grew at a more modest but accelerating median rate of 9.1%. Due to PPP forgiveness, C&I loan growth remained negative year-over-year.
+ IntraFi Network's 3Q22 survey also found that 56% of bank executives expected loan demand to weaken prospectively, up slightly from 49% in late June and sharply from 27% in early April.

Median Net Loan Growth, Twelfth District

1−quarter % change (not annualized), excluding PPP



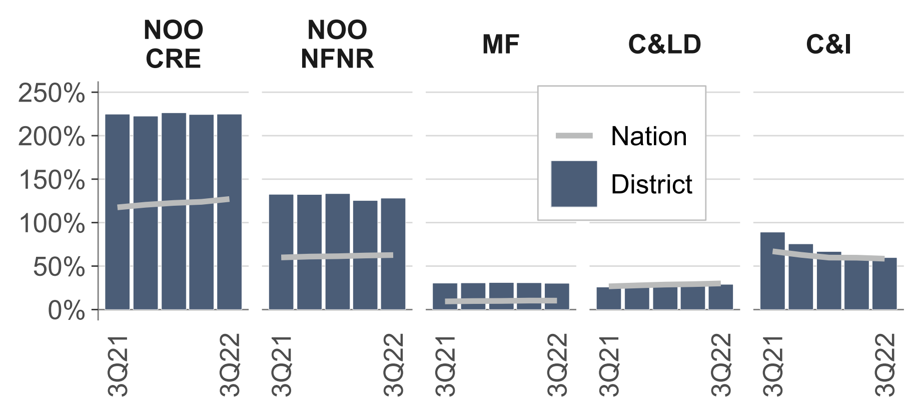
Growth rates include changes from mergers as well as organic growth. Source: Bank Call Reports/UBPRs.

CRE loan concentrations remained high but stable.

+ District bank loan portfolios continued to center in CRE categories, including those backed by owner-occupied (OO) and nonowner-occupied (NOO) collateral.
+ At 225%, the District's median NOO CRE concentration ratio – which includes NOO NFNR, MF, C&LD, and other CRE purpose loans – continued to far exceed a national median of 127% (see chart).
+ Separately, OO CRE mortgages represented 87% of tier 1 capital plus allowances in the District, also above a national median of 58%.
+ Overall C&I loan concentrations held by District banks edged lower. PPP loan concentrations (generally included within C&I) were essentially zero at most District banks, down from a mid-2020 median peak of 82%. Per the Small Business Administration, 96% of PPP funds had been fully or partially forgiven nationwide through October 2.

Median Loan Concentrations

% of tier 1 capital + ALLL or ACL



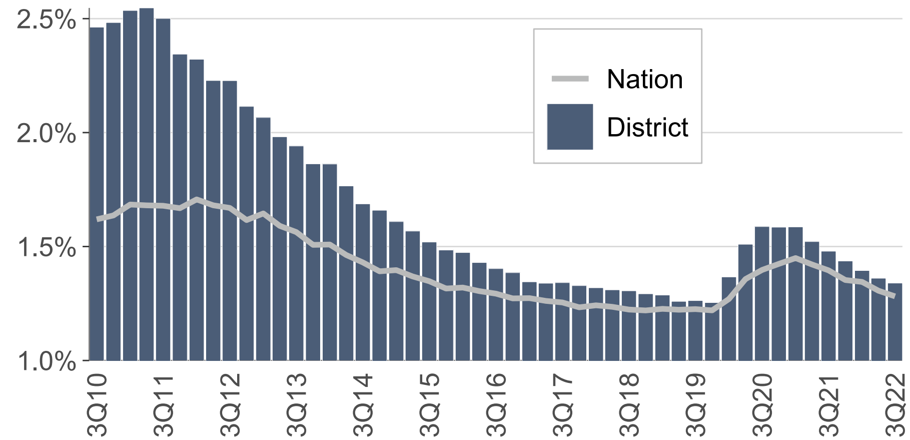
Source: Bank Call Reports/UBPRs.

Twelfth District Banking Conditions | Allowances + Underwriting

Median allowance coverage of non-PPP loans continued to recede.

- Non-PPP loan growth continued to outpace provisions for credit losses. As a result, the ratio of ALLL (or ACL)-to-non-PPP loans slid 2 bps to a median of 1.34%. District banks' coverage remained slightly above a likewise-waning national median of 1.28% (see chart).
- In the District, median coverage ratios among Very Small (1.40%) and Small (1.31%) District banks were higher than among Mid-Sized (1.07%) banks. Notably, Mid-Sized firms generally hold higher SFR loan concentrations, which are often accorded lower allowance cushions within banks' allowance methodologies.
- Allowance coverage ratios could increase if banks' views of the economic outlook deteriorate materially, particularly among CECL adopters which are required to take a longer view of future credit conditions.

Median ALLL or ACL / Non−PPP Loans & Leases not HFS

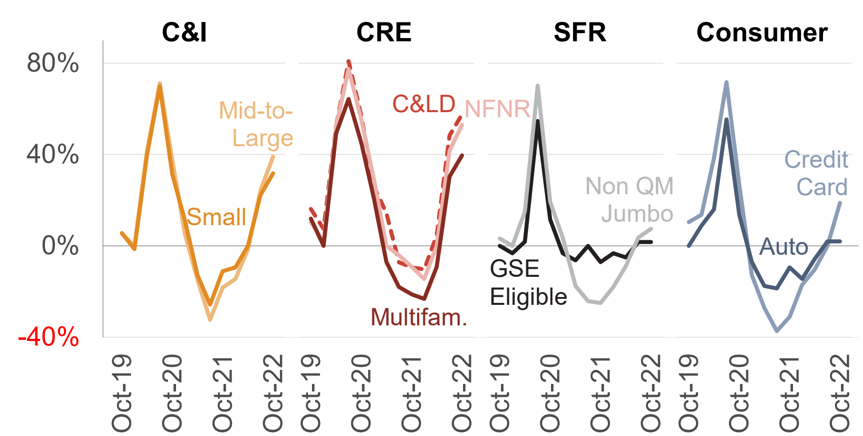


Limited to loan and lease related allowances. Source: Bank Call Reports/UBPRs.

Nationally, a notable share of lenders tightened standards; a recession could bring further tightening.

- Per the Federal Reserve's [October 2022 Senior Loan Officer Opinion Survey (SLOOS)](), a growing share of lenders tightened standards for C&I and CRE loan categories (see chart). A less favorable or more uncertain economic outlook tended to factor most heavily into the decision to tighten C&I standards. Meanwhile, reports of weakening CRE and C&I loan demand became more widespread.
- Lending to households also shifted, albeit less significantly. A modest share of banks tightened standards on certain types of residential mortgage and consumer loans compared with the prior quarter and SFR mortgage demand sank further.
- The [October SLOOS]() also found that 71% of respondents felt any near-term recession would be at least "moderate." Consistent with historical recession-era trends, 74% to 86% of those surveyed would tighten standards – primarily "somewhat" rather than "substantially" – across five major categories in the event of a downturn.

Net Percent Reporting Tighter (Easier) Loan Standards
% of surveyed loan officers



Share reporting tighter minus share reporting easier standards during the quarter. Source: Federal Reserve SLOOS via Haver Analytics.

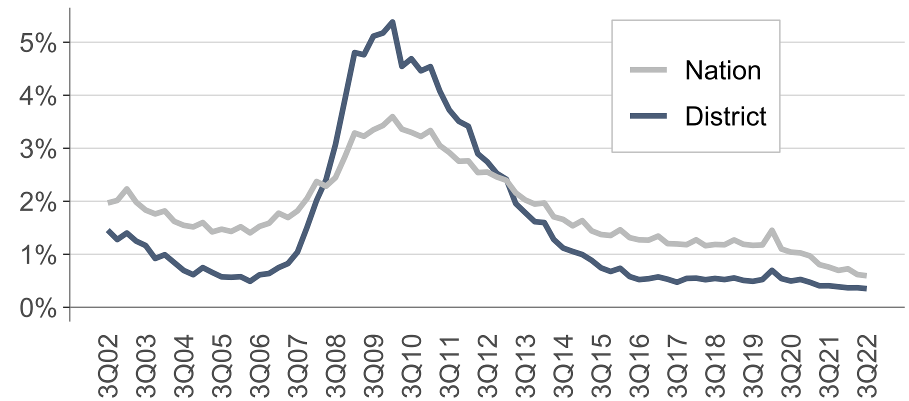
Twelfth District Banking Conditions | Loan Performance

Loan delinquencies remained low.

+ District banks' median noncurrent loan ratio – which includes credits 90+ days delinquent or on nonaccrual – edged down to just 0.17% as of September 30 (adjusted for PPP). It marked a record low for third quarters in more than 20 years of data reviewed.
+ Including 30-89 day delinquencies, the District's median overall past due non-PPP loan ratio eased to 0.35%, and outperformed a (declining) national median of 0.60% (see chart).
+ Overall delinquency rates tended to be comparable across community and Mid-Sized banks based in the District. In contrast, the median past due loan rate at Large banks nationwide ticked up to a comparatively high 1.17%, in part because of their more retail-oriented loan portfolios.
+ Credit performance may deteriorate prospectively if the economy slows significantly, especially given rising debt service burdens.

Median Past Due Loan Rates

Excluding PPP loans



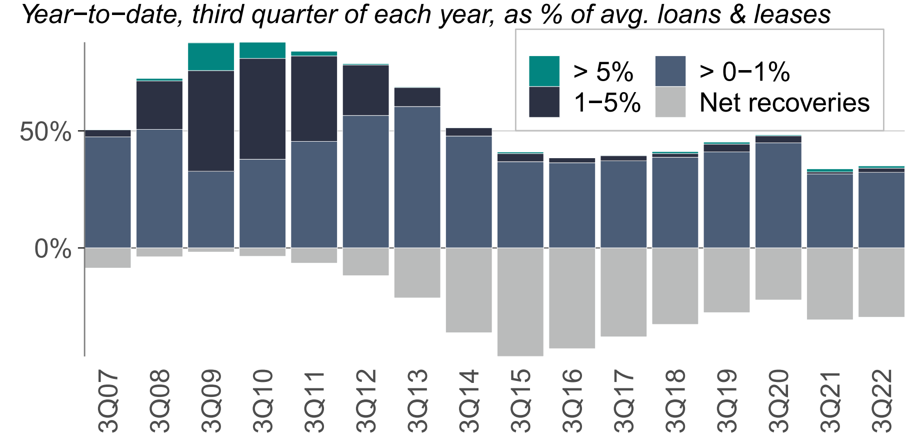
Past due includes 90+ days or nonaccrual (noncurrent) plus 30-89 days past due. Source: Bank Call Reports/UBPRs.

Net chargeoff activity remained limited.

+ Less than half of District banks (43%) recorded net loan losses through the first nine months of 2022, and a smaller share reported net loan recoveries compared with the same period in 2021 (see chart). Among those with losses, annualized chargeoff rates were predominantly below 1%.
+ Net chargeoff activity could worsen should the economy slow. The 3Q22 [CSBS Community Bank Sentiment] found that 57% of bankers in the "West" expected business conditions to worsen in the coming 12 months. Likewise, [IntraFi Network] found that 52% of bank executives believed the U.S. economy was already in recession or would be by the end of 2022. Another 36% expected a downturn during the first half of 2023 and 11% felt it would occur in the second half of the year.

Share of Banks with Net Chargeoffs, Twelfth District

Year–to–date, third quarter of each year, as % of avg. loans & leases



Source: Bank Call Reports/UBPRs.

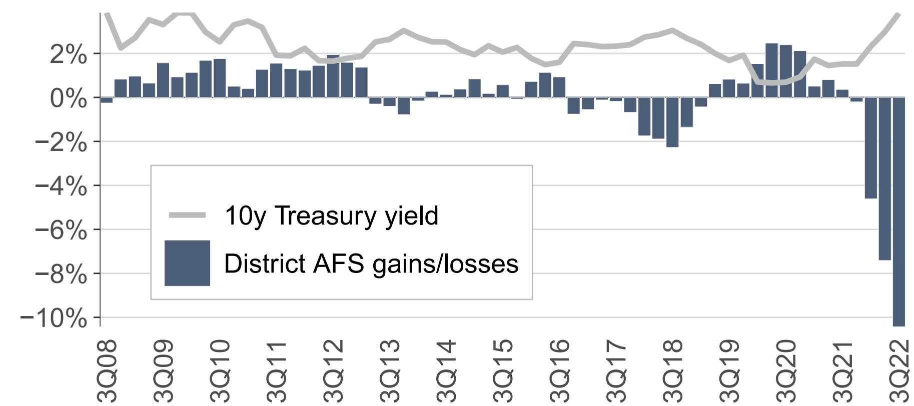
Twelfth District Banking Conditions | Liquidity

On-balance sheet liquidity slipped and bond values sank further.

- Many banks deployed excess liquidity into loans. As a result, median cash, securities, and other liquid instruments edged lower as a share of assets but continued to exceed pre-pandemic levels.
- Declines in bond valuations, including among AFS securities, intensified amid rising long-term interest rates (see chart). This further eroded accumulated other comprehensive income (AOCI) within capital accounts, which captures such losses. AOCI declines often weighed most heavily on Mid-Sized banks, which tended to invest more heavily in AFS securities as a share of assets.
- In addition to crimping on-balance sheet liquidity, net unrealized losses on bonds may affect borrowing capacity. In particular, Federal Home Loan Bank (FHLB) rules may restrict a bank's ability to obtain or renew borrowings should "tangible capital" – including AOCI adjustments – drop below zero.

Median Net Unrealized Gains (Losses) on AFS Securities

% of portfolio value

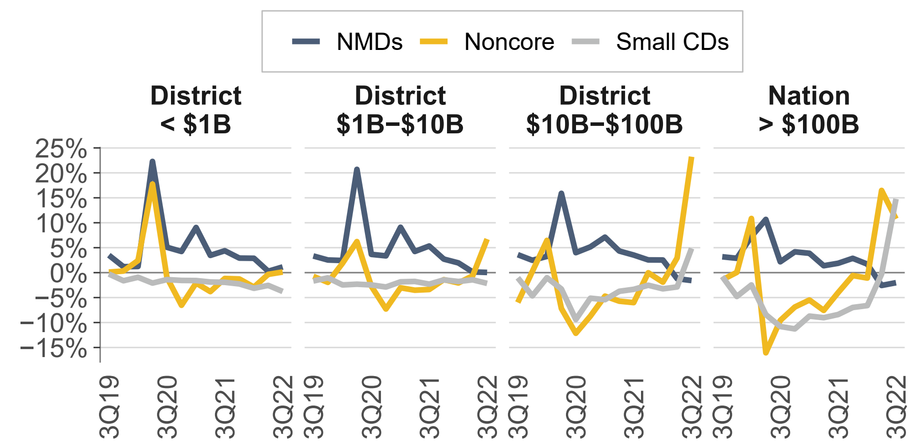


Source: Bank Call Reports/UBPRs.

Quarterly NMD growth ticked higher at smaller banks, other sizes leaned increasingly on noncore funding.

- Median quarterly NMD growth totaled 28 bps among the District's banks, up from 7 bps in the prior quarter, likely influenced in part by seasonal patterns. Pre pandemic, quarterly NMD growth tended to accelerate in the first and third quarters of each year.
- Overall NMD trends varied by bank size. Unlike smaller banks, Mid-Sized District banks and Large banks nationally reported declines in NMD volumes on a median basis for the second quarter in a row. Meanwhile, they reported notable increases in small CDs and noncore liabilities (see chart). Still, median noncore liability-to-asset ratios remained below pre-pandemic levels among the District's Very Small (4.2%), Small (5.2%), and Mid-Sized (11.4%) banks.
- NMDs remained a key source of funding, supporting 79% of District bank assets on a median basis. Jumbo NMDs – accounts exceeding $250K each – supported nearly half of banks' assets in the District versus a U.S. median of 32%.

Median Quarterly Liability Growth by Bank Size



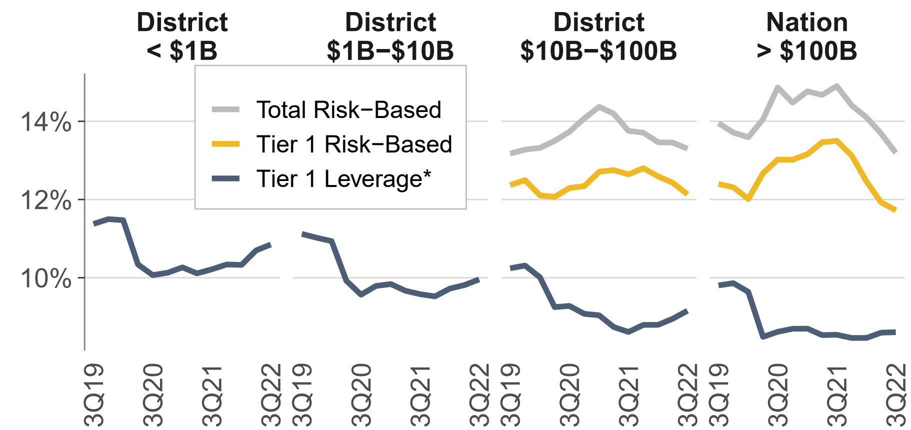
Noncore includes CDs > $250K, smaller brokered funds, foreign deposits, fed funds purchased/repos, plus borrowings. Source: Bank Call Reports/UBPRs.

Twelfth District Banking Conditions | Capital

Regulatory capital ratios moved higher in some cases, with performance varying by bank size.

+ Districtwide, the median tier 1 leverage ratio was 10.23%, up 29 bps from 2Q22, fueled by earnings-driven capital accretion and modest asset growth (see chart).
+ Meanwhile, median tier 1 and total risk-based capital (RBC) ratios increased 21 bps and 34 bps, respectively, quarter-over-quarter, led by improvements among the District's community banks. Notably, median RBC ratios slipped at Mid-Sized banks in the District and Large banks nationally, led by dividend payouts and/or loan-driven growth in risk weighted assets, continuing an earlier trend.
+ Except at large firms, AOCI is generally ignored for federal regulatory capital measures via "opt-out" provisions, but the FHLB and some states have rules tied to "book" capital. Regardless, net unrealized investment losses are a reality and financial and contractual risks to banks and their affiliates should be fully understood.

Median Regultory Capital Ratios by Bank Size



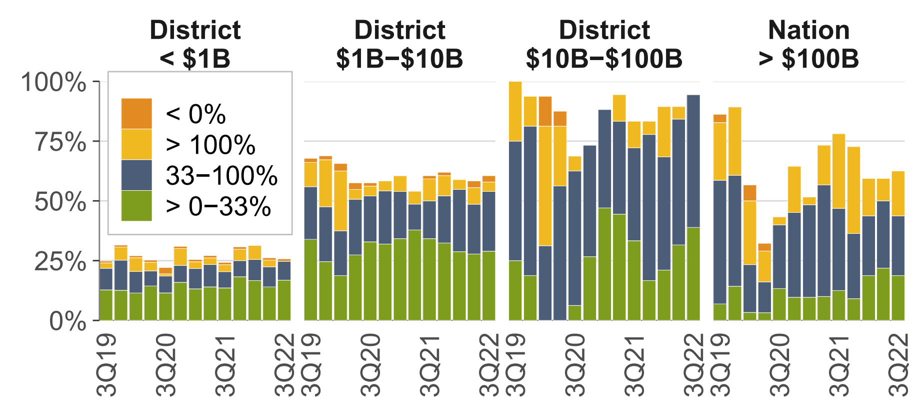
*Includes community bank leverage ratio (CBLR) reporters. Source: Bank Call Reports/UBPRs.

Less than half of District non-Subchapter S banks paid dividends.

+ Among the District's non-Subchapter S banks, roughly 46% paid dividends in 3Q22, up slightly from the second quarter. Dividend payouts remained least common among Very Small banks and most common among Mid-Sized banks (see chart).
+ At about one quarter of non-Subchapter S banks, dividend payouts represented less than one-third of net income. Another 19% paid dividends that were higher than that but less than net profit, and 4% paid dividends in excess of quarterly net income.
+ Stronger profits helped boost capital accretion rates at most banks. On a median basis, 3Q22 retained earnings-to-average equity ratios improved quarter-over-quarter to 11.2%, 12.2%, and 7.0% among Very Small, Small, and Mid-Sized banks based in the District, respectively. The slower pace of capital accretion at Mid-Sized banks was a function of comparatively higher dividend payouts.

Cash Dividends by Bank Size

Share of C–corp banks paying dividends, as % of quarterly net income



Excludes banks with Subchapter-S tax treatment, which distribute funds to cover owners' taxes. Source: Bank Call Reports/UBPRs.

Appendix | Technical Information + Abbreviations

Summary of Institutions by State & Technical Notes

Area	Commercial Banks (De Novos)		Industrial Banks (De Novos)		Savings Institutions (De Novos)	
	Sep-22	Sep-21	Sep-22	Sep-21	Sep-22	Sep-21
Alaska	4 (0)	4 (0)	-	-	1 (0)	1 (0)
Arizona	15 (3)	13 (0)	-	-	1 (0)	-
California	118 (2)	127 (1)	3 (0)	3 (0)	9 (0)	10 (0)
Guam	2 (0)	2 (0)	-	-	1 (0)	1 (0)
Hawaii	4 (0)	4 (0)	1 (0)	1 (0)	2 (0)	2 (0)
Idaho	10 (0)	10 (0)	-	-	1 (0)	1 (0)
Nevada	11 (0)	11 (1)	4 (0)	4 (0)	2 (0)	2 (0)
Oregon	13 (0)	13 (0)	-	-	2 (0)	2 (0)
Utah	25 (1)	27 (1)	15 (2)	16 (2)	1 (0)	1 (0)
Washington	34 (0)	32 (0)	-	-	7 (0)	8 (0)
District	236 (6)	243 (3)	23 (2)	24 (2)	27 (0)	28 (0)
Nation	4,132 (29)	4,274 (30)	24 (2)	26 (2)	589 (0)	613 (0)

Based on preliminary 3Q22 data (Call Reports filed through November 8, 2022).

- General: This report focuses on the financial trends and performance of commercial banks supervised by or headquartered within the Twelfth 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. Beginning in 1Q22, statistics are predominantly shown on a median rather than a "trimmed average" basis, so comparisons with prior editions of this report should be made with caution. 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, most graphics exclude "De Novo" banks (less than three years old), 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 <$1 billion, $1-$10 billion, and $10-$100 billion, respectively. The "Large" bank group uses banks with assets >$100 billion nationwide because these banks typically operate beyond the District's geographic footprint and a larger statistical population is preferred for medians and trimmed averages.

Common Abbreviations

AFS	available for sale
ACL	allowance for credit losses
ALLL	allowance for loan and lease losses
BSA/AML	Bank Secrecy Act/anti-money laundering
C&I	commercial & industrial
C&LD	construction & land development
CBLR	community bank leverage ratio
CD	certificate of deposit
CECL	current expected credit loss
CRE	commercial real estate
HFS	held for sale
MF	multifamily (5+ unit housing)
MMDA	money market deposit account
NFNR	nonfarm-nonresidential
NMD	nonmaturity deposit (excludes CDs)
PPP	Paycheck Protection Program
ROAA	return on average assets (net income/average assets)
SFR	single-family residential (1-4 family housing)
TE	tax equivalent
YTD	year to date