Economic and Banking Performance
in the Twelfth Federal Reserve District

# First Glance 12L

## Banks Faced a Challenging Funding Landscape

**1Q23**

June 1, 2023

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**: Overall, District job growth improved slightly during 1Q23, and unemployment rates edged lower in most District states. Home prices, permit activity, and homebuilder sentiment seemed to respond favorably to an early-2023 dip in mortgage interest rates and low inventories of existing homes for sale. Notwithstanding some month-over-month improvements, prices, permits, and sentiment generally trailed year-ago levels. Meanwhile, commercial real estate (CRE) markets remained under pressure, particularly in the office sector. Generally, CRE owners faced flat or declining property prices, weakening demand, tightening credit conditions, and/or rising debt service costs and operating expenses.

**Banking Conditions**: Banks encountered a challenging funding environment during the quarter. Nonmaturity deposit runoff continued, especially in March following the failure of two large depositories. Banks leaned increasingly on time deposits (including brokered funds) and borrowing lines and strengthened cash buffers in response. Institutions remained solidly profitable, but the combination of rising short-term interest rates, competitive pricing pressures, and shifts in funding mix pushed interest expenses up faster than asset yields, compressing margins. Seasonal and other increases in overhead expenses also detracted. Although moderating, net unrealized losses among bond portfolios influenced depositor and investor behavior and concurrently constrained banks' liquidity options. Loan delinquencies and losses remained low. Still, surveyed bankers expressed continuing caution about the economy.

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A product of SF Fed | Supervision + Credit

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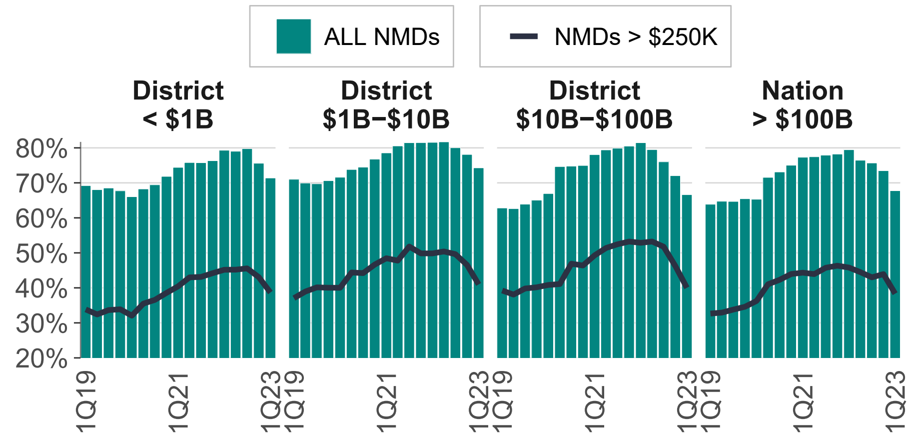
# Issues on Our Radar | Selected issues we are watching most closely

## Shifts in funding mix and cost

+ Deposits, particularly low cost nonmaturity deposits (NMDs) grew in 2020 and 2021, led by flight-to-safety and stimulus-related funding. However, NMD attrition accelerated after mid-2022 as depositors responded to lagged deposit repricing and, more recently, bank failures (see chart). Large depositors (e.g., above $250 thousand) contributed to the magnitude of growth and runoff since 2019.
+ Firms turned to pricier sources to replace withdrawals. By March 31, “noncore” jumbo CDs, small brokered deposits, borrowings, federal funds purchased, repurchase agreements, and foreign deposits had increased to 11.3% of District banks’ assets, up from 4.5% in early 2022. Among Mid-Sized District banks (assets of $10 billion to $100 billion), the median ratio nearly quadrupled to 19.8% over the year.
+ Funding costs incurred over the course of 1Q23 only partially reflect the impact of funding stress faced late in the quarter.

**Median Nonmaturity Deposits / Total Assets by Bank Size**



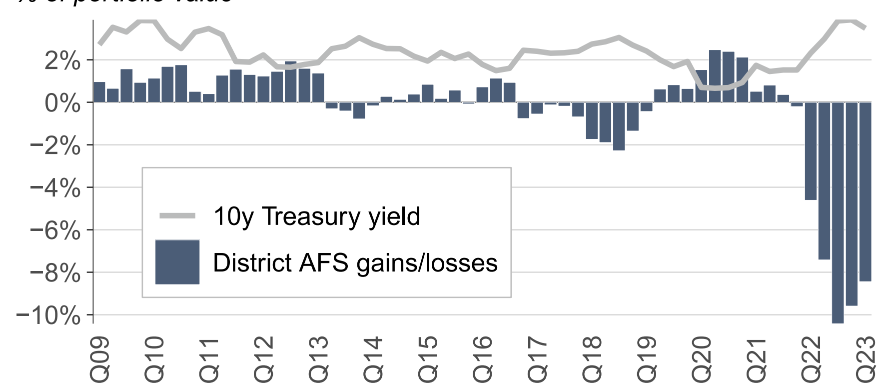

Nonmaturity deposits (NMDs) include checking, money market, and passbook type accounts but excludes time deposits. Source: Bank Call Reports/UBPRs.

## Investment portfolio valuation trends

+ Given ample deposit inflows but muted loan demand early in the pandemic, banks invested in longer-duration securities. However, by 2022, rising interest rates caused unrealized losses to accumulate among bond portfolios.
+ For AFS securities, unrealized losses reduced accumulated other comprehensive income (AOCI) within “book” capital. Unrealized losses remained significant but have receded since 3Q22 amid declining intermediate-/long-term interest rates (see chart).
+ Risks to capital posed by declining bond values increasingly caught the attention of investors and depositors in March 2023 following the failures of two Large banks (assets above $100 billion). This amplified funding challenges among some banks.
+ Simultaneously, unrealized losses narrowed banks’ options for raising liquidity to fund deposit outflows.

**Median Net Unrealized Gains (Losses) on AFS Securities**

*% of portfolio value*




AFS = available for sale. Sources: U.S. Treasury via Haver Analytics; Bank Call Reports/UBPRs.

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

## Real estate loan concentrations

- Banks in the West engage heavily in real estate lending, in particular commercial real estate (CRE) mortgages. The District's median CRE loan-to-capital and allowances ratio of 337%, led by banks based in California and Arizona, far surpassed a national median of 203% (see table).
- Rising interest rates may pressure repayment capacity or hamper collateral values if higher financing costs are not offset by a corresponding increase in net operating income. In particular, loans with balloon payments maturing in the near-term may face refinancing risk. Challenges may be most pronounced among office collateral, particularly if located in downtown areas, as further discussed on pages 9 to 11.
- 1-4 family mortgage (SFR) concentrations edged up further. Exposures tend to be higher among the District's Mid-Sized than community banks (assets below $10 billion). Slowing economic conditions could affect demand for and performance of SFR and residential C&LD loans, especially given price property price pressures.

## C&I credit risks

- As of 1Q23, District banks' commercial and industrial (C&I) loan balances represented 53% of tier 1 capital plus allowances on a median basis.
- Although low overall, C&I loan delinquencies and net chargeoffs edged higher in 1Q23 among some District banks. Economic slowing or rising input and debt service costs may challenge some C&I borrowers.
- Leveraged loans, which predominantly have variable interest rates, continue to pose heightened risks (see Shared National Credit results).

## Current Expected Credit Loss (CECL) implementation

- In 1Q23, 78% of District banks – mainly small, non-publicly traded firms – adopted the CECL allowance method. Most reported mild if any "Day 1" impacts, with adjustments flowing through capital directly (see page 14).
- The Federal Reserve's CECL Resource Center offers resources, 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 + ACL
*March 31, 2023*

| | Total CRE | NOO CRE |
|---|---|---|
| **California** | 371% | 274% |
| **Arizona** | 349% | 228% |
| **Washington** | 337% | 238% |
| **Oregon** | 296% | 213% |
| **Nevada** | 292% | 167% |
| **Alaska** | 255% | 173% |
| **Idaho** | 236% | 165% |
| **Hawaii** | 226% | 165% |
| **Utah** | 175% | 105% |
| **Nation** | 203% | 131% |

Based upon state of bank headquarters; commercial real estate (CRE) includes owner- and nonowner-occupied (NOO) nonfarm-nonresidential (NFNR), multifamily, construction and land development (C&LD), and other CRE purpose loans; NOO CRE excludes owner-occupied NFNR mortgages. Sources: Bank Call Reports/Uniform Bank Performance Reports (UBPRs).

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

## Cybersecurity

+ Cyber remains a top risk given an ever-growing multitude of threats, particularly amid evolving geopolitical developments. Ransomware with double extortion, phishing campaigns, API security misconfiguration, patch management, rising cyber insurance premiums, and supply chain compromises are the primary cyber issues facing supervised institutions, their customers, and their suppliers. The increase in digital financial services and mobile banking has exponentially expanded the attack surface that criminals can exploit.
+ Cloud computing adoption continued to increase, escalating the need for effective risk and vendor management programs. The U.S. Treasury released a report on February 8 about the potential benefits and challenges of cloud adoption, which included recommendations for safe, secure, and responsible usage.
+ In mid-April 2023, the Financial Stability Board updated the Cyber Lexicon to remain current with the evolving cyber and information technology landscape and to achieve greater consistency in cyber incident reporting.
+ Firms are addressing compliance and security concerns related to artificial intelligence (AI) by either restricting or blocking the use of AI tools by employees. In January 2023, the National Institute for Standards and Technology released an AI Risk Management Framework (AI RMF 1.0), for voluntary use by organizations designing, developing, deploying or using AI systems.

## Enterprise complexity due to novel activities

+ Networks of multiple complex third/fourth party relationships stemming from the adoption of crypto-asset services, bank-fintech partnerships (such as Banking-as-a-Service models), and other novel activities are drivers for heightened concern.
+ Vulnerabilities can be compounded if revenues, funding, or assets are concentrated in a novel business line or if the risk appetite for engaging with nonbank partners gets ahead of the control environment.
+ Given developments in the marketplace and attendant risks, the banking agencies issued several pieces of guidance in 1Q23 related to crypto-asset and other novel business models, including a Joint Statement on Crypto-Asset Risks to Banking Organizations on January 3, a Federal Reserve Policy Statement to Promote a Level Playing Field for All Banks with a Federal Supervisor on January 27, and a Joint Statement on Liquidity Risks Resulting from Crypto-Asset Market Vulnerabilities on February 23.

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

## 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 digital asset related services, and the evolving nature of threats and regulatory guidance.
+ FinCEN issued several notices during 1Q23. On February 27, FinCEN alerted financial institutions to a nationwide surge in check fraud schemes targeting the U.S. Mail. Then in March, they published the first set of guidance to aid the public in understanding upcoming beneficial ownership information reporting requirements, which will take effect on January 1, 2024. Lastly, FinCEN renewed and expanded Geographic Targeting Orders in late April, which require U.S. title insurance companies to identify natural persons behind shell companies used in non-financed purchases of residential real estate.

## Consumer compliance regulatory developments

+ In March 2023, the Consumer Financial Protection Bureau (CFPB) finalized its Small Business Lending Data Collection rule, which will have a phased-in effective date based upon the number of covered originations in 2022 and 2023. Larger originators are required to begin collecting data on October 1, 2024.
+ Also pending is the Interagency Community Reinvestment Act (proposed in May 2022), which is expected to be finalized this year.
+ In January 2022, the CFPB launched an initiative to identify "exploitative junk fees," which resulted in guidance related to debt collection "pay-to-pay" fees and overdraft/returned deposited item fees. Relatedly, in early February, the agency proposed a rule to curb excessive credit card late fees.

## LIBOR transition

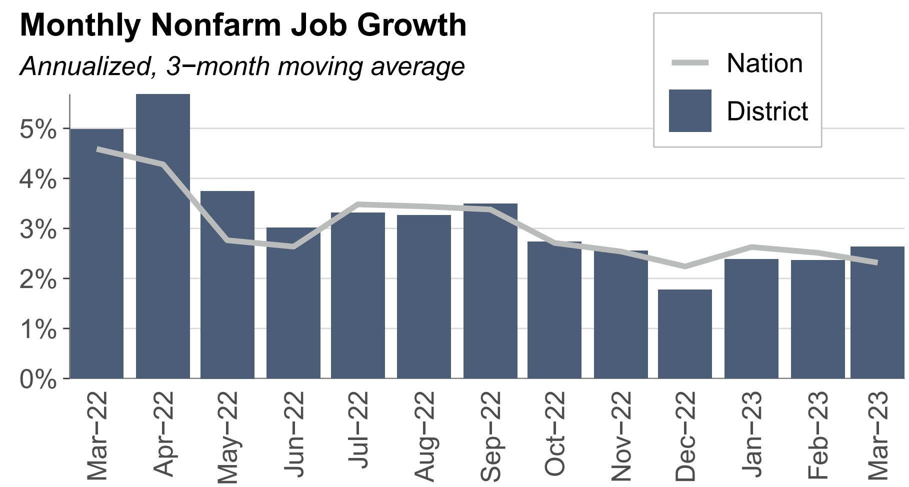
+ LIBOR transition will remain an area of focus ahead of the mid-2023 sunset of LIBOR. The Federal Reserve's LIBOR Transition website provides guidance on instruments with tenors beyond June 2023, which may require renegotiation, fallback language, and/or an alternative reference rate.
+ The banking agencies issued a joint statement in April 2023 regarding the importance of transitioning remaining contracts expeditiously. Alternative reference rates should be appropriate for the bank's products, its risk profile and capabilities, and its customers' needs. Reference rate construction and fragilities should be understood.
+ Exposure is generally low among most District banks, primarily via securities, derivatives, and/or subordinated debt. LIBOR-based lending is limited.

*See the Federal Reserve's semi-annual reports on Supervision and Regulation and Financial Stability to learn more about key risk issues.*

# Twelfth District Economy | Employment

## Job growth re-accelerated mildly in early 2023.

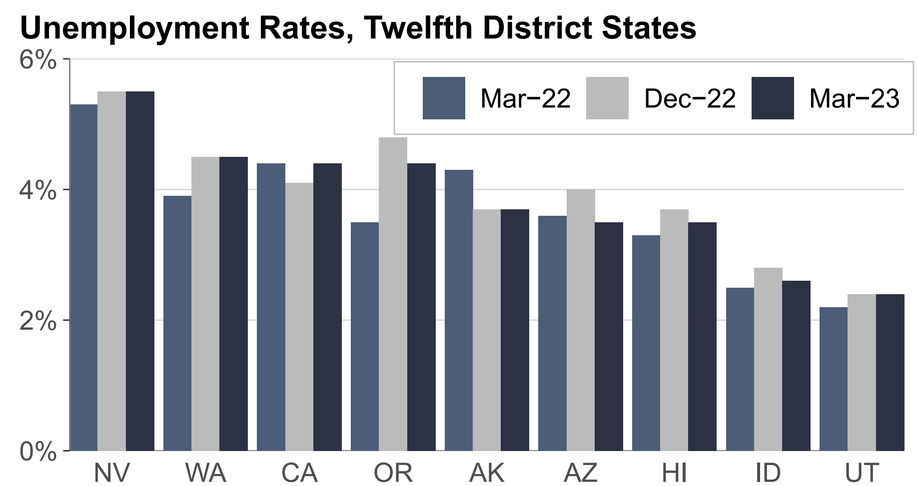
- On average, job growth improved through March, edging up to 2.63% (annualized, three-month moving average basis). The District slightly outpaced an average nationwide rate of 2.32% (see chart).
- The leisure/hospitality and education/health sectors continued to be important drivers of new hiring. Unlike late 2022, the government and retail trade sectors boosted seasonally-adjusted payrolls. Meanwhile, the construction, financial activities, information (media and some tech-related jobs), and wholesale trade sectors shed payrolls on average.
- Among the District's states, 1Q23 job growth was strongest (on an average monthly annualized basis) in Idaho (4.53%), Nevada (4.09%), Utah (3.82%), Hawaii (3.73%), and Washington (3.36%). Meanwhile, average growth was negative in Alaska (-0.91%) where payrolls, along with Hawaii's, still trailed pre-pandemic (Feb. 2020) levels.




Seasonally adjusted. Source: Bureau of Labor Statistics.

## Most state unemployment rates were stable-to-lower during 1Q23, with California a notable exception.

- On a seasonally-adjusted basis, the Districtwide unemployment rate ticked higher to 4.21% in March, up from 4.12% in December, mainly because of an increase in unemployment in California (+69K persons). The District's aggregate jobless rate remained above a stable nationwide rate of 3.50%.
- Other than California, state level unemployment rates in the District were stable-to-lower over the three month period (see chart).
- Jobless rates in Nevada, Washington, Oregon, and California, each of which topped 4.40%, were among the highest in the nation, while Utah and Idaho ranked among the lowest.




Seasonally adjusted. Source: Bureau of Labor Statistics.

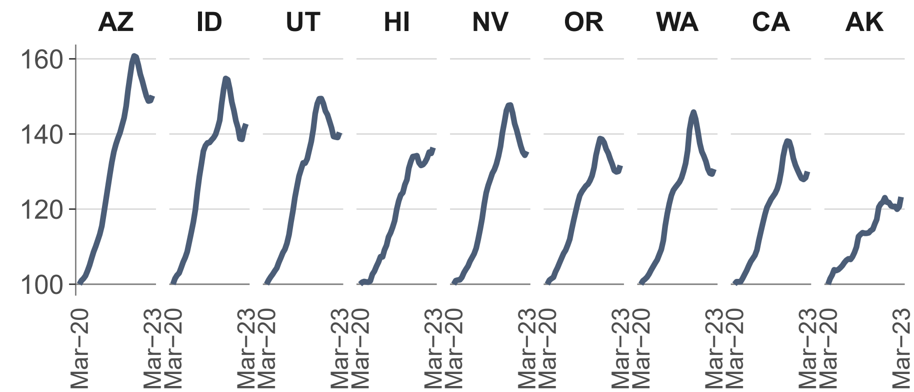
# Twelfth District Economy | Housing

## The home price slide took a breather in early 2023.

- Per CoreLogic, single-family home price indices (HPIs) peaked in most District states around mid-2022 and then weakened during the second half of the year. By February 2023, prices improved slightly month-over-month in most states, likely influenced by moderating mortgage interest rates and tight for-sale inventories (see chart).
- Although stronger on a monthly basis, March 2023 HPIs trailed year-ago levels in all contiguous District states. Washington's HPI fell the most over the 12-month period, led by a 12.8% drop in Seattle-area prices. Annual percentage point declines were also in the double digits among expensive areas like the San Francisco Bay Area, where rising interest rates and tech layoffs weighed on prices.
- Prices remained well above March 2020 levels, most notably in Arizona (+50%), Idaho (+43%), and Utah (+40%), where earlier gains were influenced by people moving in from higher cost markets.

**Home Price Index, Twelfth District States**

*Mar−20 = 100*



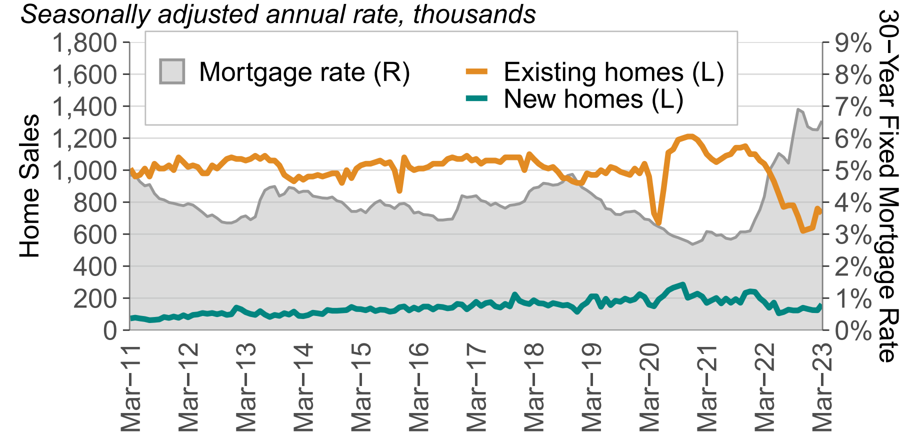

Index covers attached and detached single-family homes, including distressed sales. Sources: CoreLogic, SF Fed calculations.

## Existing home sales edged up, but higher mortgage rates, low inventories, and economic uncertainty pose headwinds.

- Existing single-family home sales in the West improved in early 2023 after dropping to a rate in 4Q22 that had not been observed in nearly 30 years. New home sales also gained strength by March but both remained below pandemic-era peaks (see chart).
- The March 2023 National Association of REALTORS® pending home sales index for the West, which leads finalized sales by one to two months, eased from earlier in the quarter. Low for-sale inventories were a factor. Future sales will remain reliant on the volume of listings, the path of mortgage interest rates, and the health of the economy.
- In addition to constraining sales volumes, tight inventories likely contributed to upward price pressures during the quarter. Data from Redfin suggests aggregate for-sale inventories in the District averaged 2.7 months' worth of sales in 1Q23, down slightly from 3.1 months in the prior quarter.

**Single−Family Home Sales, West Region**

*Seasonally adjusted annual rate, thousands*

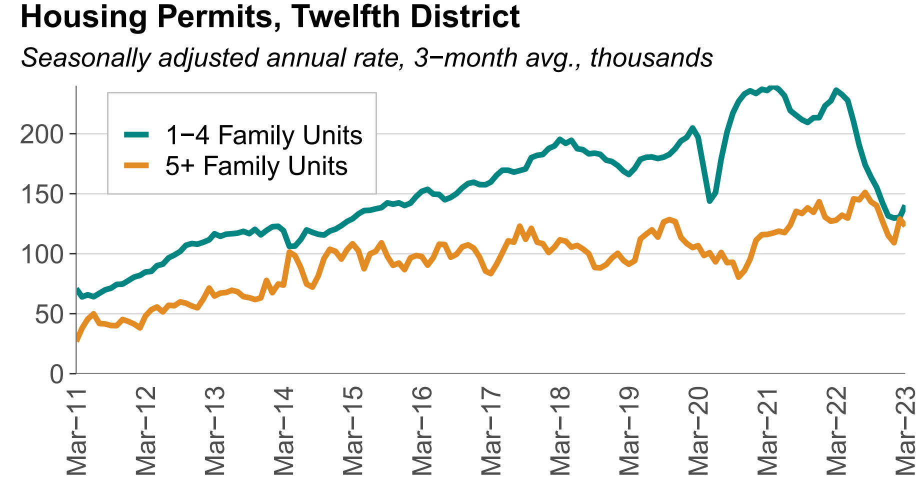



West = District plus CO, MT, NM, and WY. Sources: National Association of REALTORS® (© 2022, reprinted with permission), Census Bureau, Freddie Mac.

# Twelfth District Economy | Housing + Commercial Real Estate

## Housing permit activity and homebuilder confidence were down year-over-year but improved from late 2022 levels.

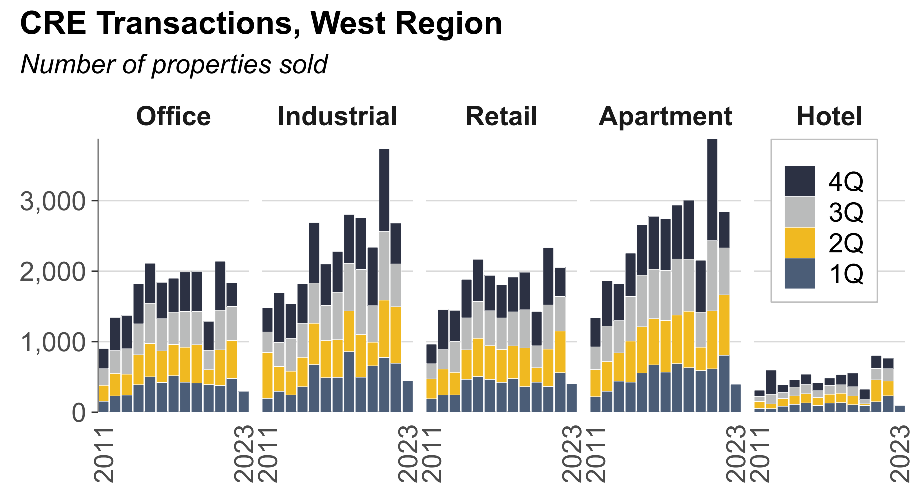
+ The District's three-month trailing average of 1-4 family housing permits perked up slightly in response to easing, albeit volatile, mortgage interest rates in early 2023 and limited resale inventory (see chart). Still, 1-4 family permit activity remained well-below strong levels recorded amid the pandemic era's low interest rates.
+ Multifamily (5+ unit) permit issuance remained comparatively volatile, trending slightly higher overall after faltering in late 2022. Recent multifamily permit lulls in Hawaii, Idaho, and Nevada were offset by increases in other District states.
+ Between December 2022 and May 2023, the West's NAHB/Wells Fargo Housing Market Index, a measure of homebuilder confidence, nearly doubled to a reading of 48. Although improved, the sub-50 index was well below the reading in May 2022 (83) and indicated slightly more homebuilders remained bearish rather than bullish.




Source: Census Bureau via Haver Analytics.

## CRE sales transaction volumes trailed 1Q22 amid higher interest rates and weakening real estate investor sentiment.

+ Per MSCI/Real Capital Analytics (RCA), CRE transaction volumes in the West lagged prior quarter, year ago, and pre-pandemic (1Q19) levels (see chart). The aggregate number of property sales in the region (all sectors) was down 41% year-over-year. However, 2022's record high first quarter deal counts partly contributed to the magnitude of year-over-year decline.
+ In addition to a normalizing pace, lower sales activity likely reflected the binding effects of higher interest rates, slowing economic activity, and divergent buyer-seller expectations.
+ National Association of Industrial and Office Properties' (NAIOP) early April 2023 CRE Sentiment Survey found that most responding CRE professionals expected market conditions to worsen over the next 12 months.




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

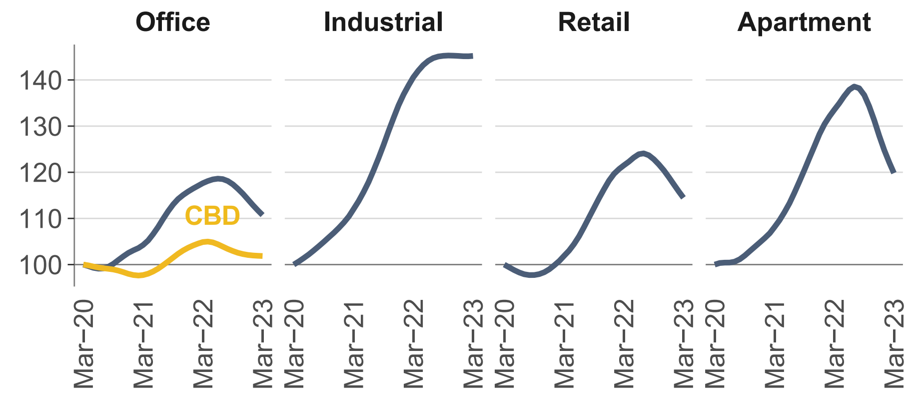
# Twelfth District Economy | Commercial Real Estate

## Property prices in most CRE sectors continued to give up gains accrued during the pandemic.

+ MSCI/RCA's national office price index ended March down 7% from its 2022 peak, with central business district (CBD) properties only slightly above their level three years prior (see chart). Persistent hybrid/remote work has weighed heavily on the sector.
+ Nationally, MSCI/RCA's apartment and retail property prices shed 14% and 8%, respectively, from their 2022 peaks (see chart). Industrial property prices, which were on a tear nationwide during the pandemic, flattened after peaking in October 2022.
+ Separately, CoStar noted that composite CRE prices in the "West" declined the most year-over-year among four major U.S. regions.
+ Rising interest rates/capitalization rates, pressures on net operating incomes, slowing economic conditions, and ongoing secular shifts (e.g., retail, office) contributed to pricing trends.

**Commercial Property Price Indices, Nation**

*Mar−20 = 100*



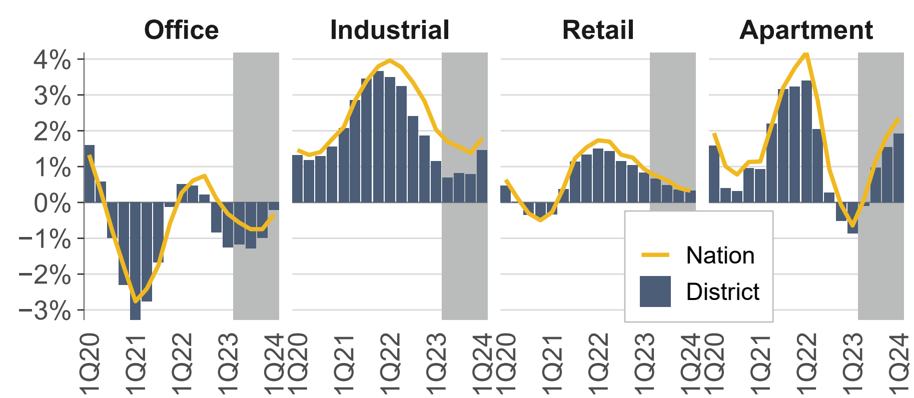

Based upon repeat-sales transactions; CBD = central business district.
Sources: MSCI/Real Capital Analytics, SF Fed calculations.

## Demand for commercial space dipped further, especially in the office and apartment sectors.

+ The trailing four-quarter absorption rate remained negative in the District's office sector in 1Q23. CBRE-EA expects office demand will remain in the doldrums given hybrid/remote work trends and weaker economic prospects (see chart).
+ Most major District apartment markets also experienced negative absorption in the 12 months ending March. However, forecast data from CBRE-EA suggests apartment absorption rates may strengthen in the coming year.
+ Industrial and retail absorption rates also slowed, with retail facing the prospect of ongoing weakening per CBRE-EA.

**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.
Sources: CBRE-EA, SF Fed calculations.

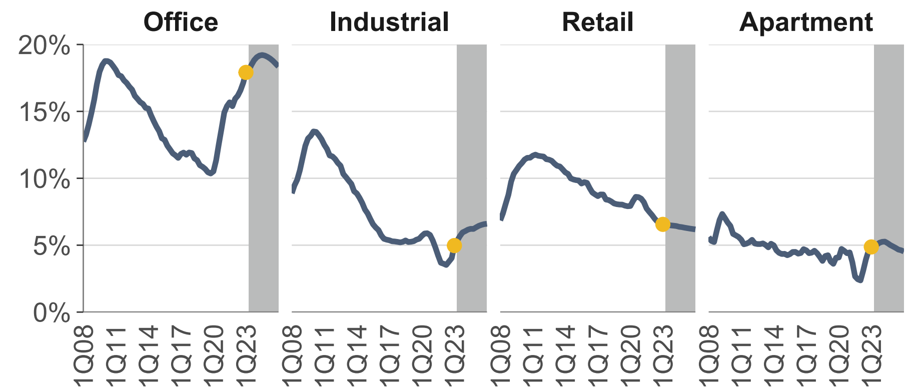
# Twelfth District Economy | Commercial Real Estate

## Vacancy rates generally drifted higher for office, apartment, and industrial properties.

+ Office vacancy rates increased across most District markets during the quarter and approached Great Recession peaks in aggregate (see chart). CBRE-EA expects office occupancy will weaken further in the near term as tenants re-calibrate space needs.
+ Although still in the low-to-mid single digits, apartment vacancies edged up in most major District markets during 1Q23. CBRE-EA does not expect an elevated pace of completions in the coming quarters to move vacancy rates materially, provided absorption rebounds.
+ Industrial space remained tight overall, with availability up from very low levels amid new construction. Industrial vacancy rates are expected to edge higher as new construction outpaces absorption.
+ Retail property vacancy rates were generally stable-to-lower quarter-over-quarter amid limited new supply.

**Avg. CRE Vacancy Rates, Twelfth District, 1Q08 – 1Q26**

*Weighted by stock, shaded area = 3–year forecast*



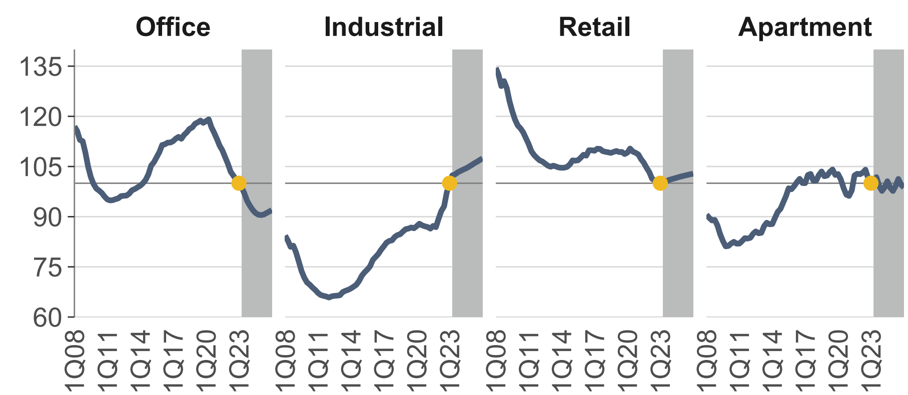

Weighted across 16 to 18 large District markets; office/apartment = vacancy rate; industrial/retail = availability rate. Sources: CBRE-EA, SF Fed calculations.

## Real commercial property rents remained under pressure outside of the industrial sector.

+ Inflation-adjusted (real) rents for office space contracted further across most District markets. CBRE-EA expects office rents to decline further – generally another 5% to 10% depending upon the market – in the coming year.
+ Real retail rents also continued to dip in just over half of the District's major metros. CBRE-EA forecasts suggest that limited availability may support retail rent growth in the near term (see chart).
+ Average real apartment rent growth slipped further across the District's major markets and may stabilize somewhat if absorption improves.
+ Meanwhile, CBRE-EA expects real industrial rents to strengthen in the near term in most District markets, albeit at a slowing pace.

**CRE Real Rent Indices, Twelfth District, 1Q08 – 1Q26**

*Weighted by stock, shaded area = 3–year forecast, 1Q23 = 100*




Weighted across 16 to 18 large District markets; office/industrial = asking rents; retail/apartment = effective rents. Sources: CBRE-EA, SF Fed calculations.

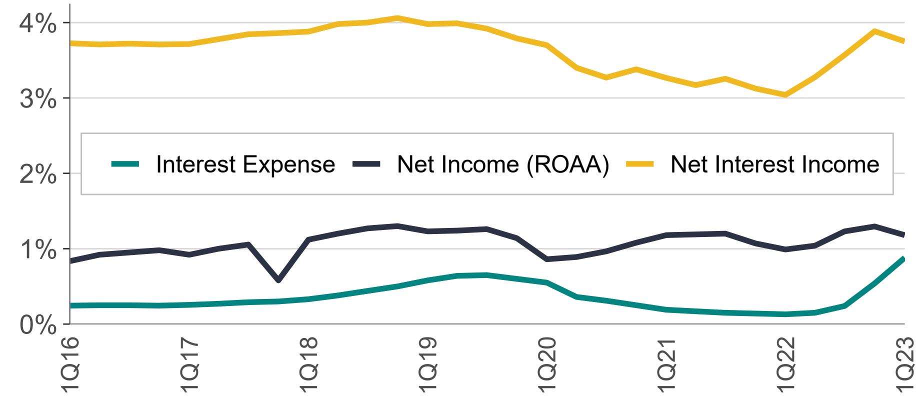
# Twelfth District Banking Conditions | Earnings

## Bank profit ratios were solid but dipped; more bankers expected earnings prospects to weaken.

+ During 1Q23, District banks earned a median quarterly return on average assets (ROAA, adjusted for Subchapter S effects) of 1.18%, down 12 bps from the prior quarter but up 19 bps from the same quarter one year ago.
+ Market disruptions in March contributed to an acceleration of deposit repricing and shifts in funding mix, a trend that had been developing in earlier quarters. On net, this reversed prior rate-driven improvements in net interest income reported during 2022 (see chart).
+ The 1Q23 CSBS Community Bank Sentiment Survey (collected throughout March) found a growing share (39%) of community bankers in the "West" expected profits to weaken in the coming year, up 10 percentage points from the prior quarter's survey. Profit concerns likely reflected worsening sentiment about business conditions, monetary policy, and regulatory burden.

**Median Earnings Ratios, Twelfth District**

*% of avg. assets, 1−quarter annualized*



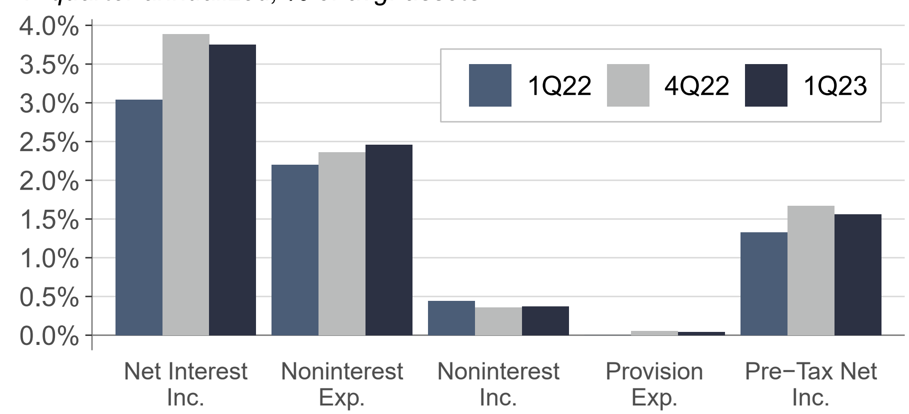

ROAA (net income / average assets) for Subchapter-S filing banks is adjusted for theoretical tax expense. Sources: Bank Call Reports/UBPRs.

## Weaker net interest income and/or higher overhead expenses drove earnings trends at most banks.

+ District banks' median one-quarter net interest income-to-average assets ratio dipped to 3.75%, down 14 bps from 4Q22. Funding costs moved higher as deposit pricing competition intensified and funding mixes shifted away from NMDs and towards costlier sources, especially among Mid-Sized banks. Asset yields also moved higher, but increases were overshadowed by rising funding costs.
+ Inflationary pressures and seasonal personnel cost factors (e.g., payroll taxes, and bonus payouts) contributed to noninterest expense increases at many banks (see chart).
+ Provision expenses edged higher at some firms. Overall, 64% of District banks incurred provision expenses during the quarter versus 63% in 4Q22 and 42% in 1Q22. Meanwhile, the share releasing reserves (6%) dropped in half quarter-over-quarter.

**Median Pre−Tax Net Income Breakdown, Twelfth District**

*1−quarter annualized, % of avg. assets*




Sources: Bank Call Reports/UBPRs.

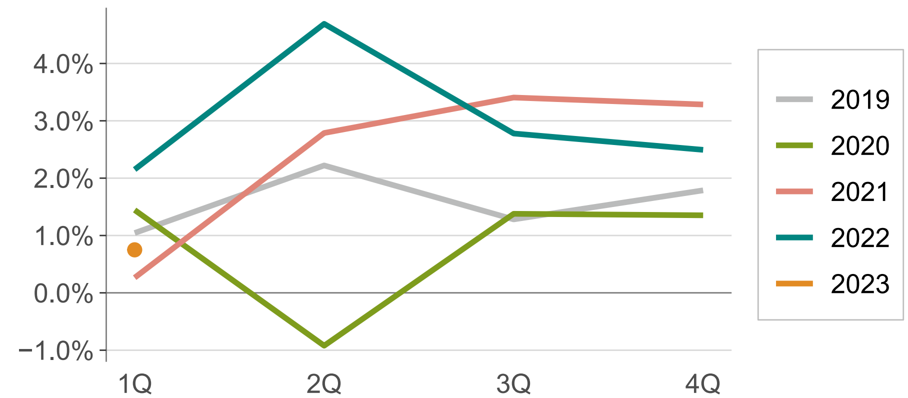
# Twelfth District Banking Conditions | Growth + Concentrations

## Annual and quarterly loan and lease growth slowed.

+ District banks' year-over-year growth in loans (excluding PPP) slowed to 11.7% on a median basis, which trailed a likewise-easing nationwide rate of 12.4%.
+ One-quarter loan growth decelerated sharply to 0.75% (not annualized), cooling from relatively robust growth rates in 2022 (see chart). The median pace of net new lending during the quarter eased across all major loan categories, mirroring a nationwide trend.
+ Lower real estate sales volumes, waning business and household sentiment, and rising interest rates likely contributed to the trend.
+ Respondents to the Fed's April Senior Loan Officer Opinion Survey and IntraFi Network's 1Q23 Bank Executive Business Outlook Survey both noted weakening loan demand. The IntraFi survey also found that 43% of bankers expected loan demand to soften prospectively.

**Median Net Loan Growth, Twelfth District**

*1–quarter % change (not annualized), excluding PPP*



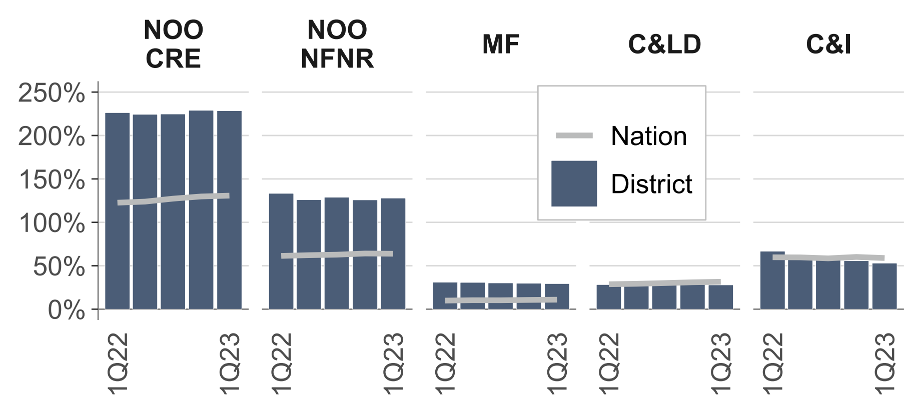

Growth rates are not merger-adjusted (include changes from mergers as well as organic growth). Sources: Bank Call Reports/UBPRs.

## CRE loan concentrations remained high and stable.

+ CRE loans, including those backed by owner-occupied (OO) and nonowner-occupied (NOO) collateral, continued to be elevated among District banks' credit portfolios.
+ At 229%, the District's median NOO CRE concentration ratio, which includes NOO NFNR, multifamily (MF), C&LD, and CRE purpose loans, remained nearly 100 percentage points above the nation (see chart).
+ Separately, OO CRE mortgages eased slightly to 83% of tier 1 capital plus allowances in the District, also above a national median of 58%.
+ SFR loans ticked higher to 57% of capital and allowances on a median basis, still less than half of a nationwide figure of 121%.

**Median Loan Concentrations**

*% of tier 1 capital + ALLL or ACL*

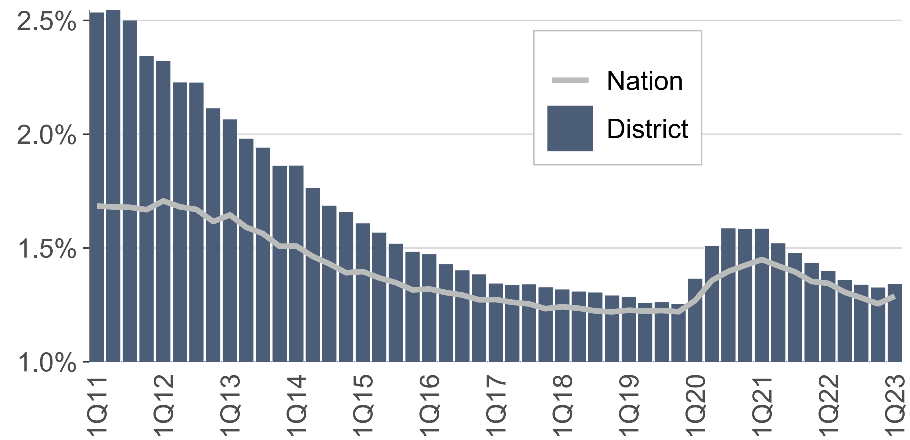



Sources: Bank Call Reports/UBPRs.

## Median allowance-to-loan ratios edged higher, driven in part by CECL adoption.

- The ratio of ALLL (or ACL)-to-non-PPP loans among District banks was 1.34%, up 1 bp from 4Q22 but down 6 bps year-over-year. District banks' allowance ratios remained slightly above the nationwide bank median, which increased 3 bps to 1.29% (see chart).
- The adoption of CECL allowance accounting by 78% of District banks during the quarter influenced the recent uptick. Among those adopting in 1Q23, 41% reported a "Day 1" increase in allowances, while 14% reported a downward adjustment, and 45% noted no "Day 1" change.
- Larger/public banks that implemented CECL in 2020 were more likely to increase allowances on "Day 1," partly because they tended to have lower pre-adoption coverage levels and larger holdings of consumer loans. Prior Federal Reserve research has found that consumer loan allowances often increased the most upon adoption.

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

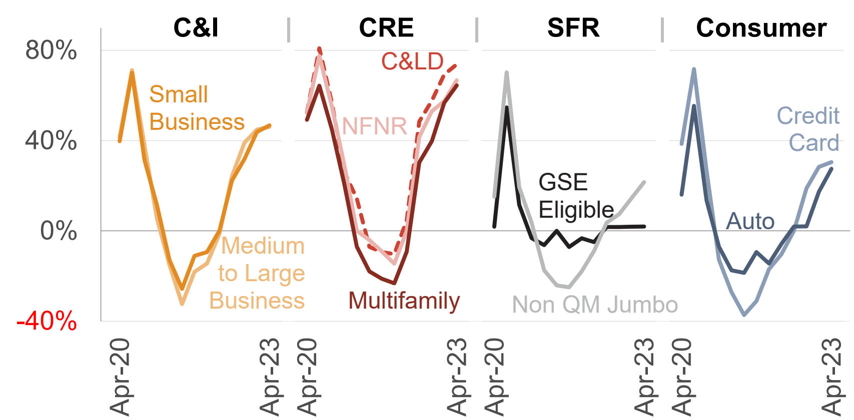



Limited to loan and lease related allowances. Sources: Bank Call Reports/ UBPRs.

## The Senior Loan Officer Opinion survey noted further credit tightening.

- Per the Federal Reserve's April 2023 Senior Loan Officer Opinion Survey, the share of lenders reporting tighter standards for C&I and CRE loans increased (see chart). Most respondents also noted ebbing CRE and C&I loan demand. Historically, tighter credit and weaker demand have preceded recessions.
- Except for GSE-eligible and government-backed mortgages, a growing share of banks tightened standards on loans to households.
- A less favorable economic outlook, reduced risk tolerance, weaker collateral values, and/or concerns about funding costs or deposit flows were frequently cited drivers of tightening. These factors, along with broader concerns about portfolio credit quality, may also crimp lender appetite over the remainder of 2023.
- Compared with last Spring, bankers most frequently required wider pricing spreads and stricter loan-to-value ratios for new CRE loans.

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




Share reporting tighter minus share reporting easier standards; QM = qualified mortgage; GSE = government sponsored enterprise. Source: Federal Reserve.

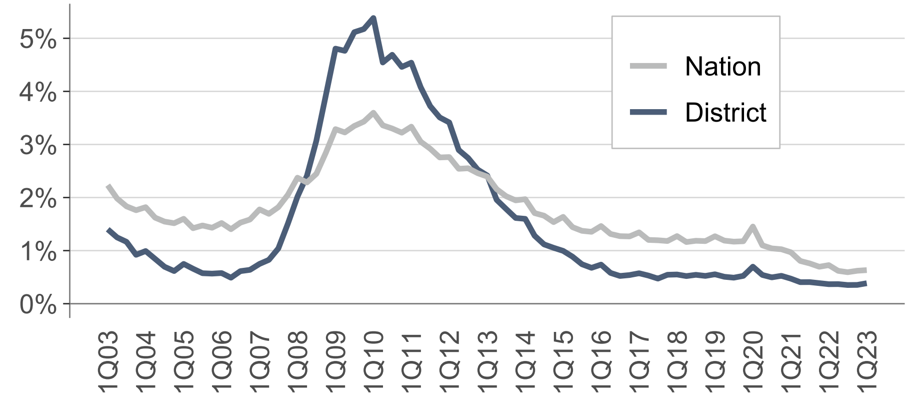
# Twelfth District Banking Conditions | Loan Performance

## Loan and lease delinquencies ticked up but remained low overall.

+ District banks' median noncurrent loan ratio — which includes credits 90+ days delinquent or on nonaccrual — edged up 3 bps to 0.17% by March 31 (denominator excludes PPP). This ranked as the mildest median noncurrent loan rate among all twelve districts and was the lowest first quarter ratio in the Twelfth District since 2006.
+ Overall delinquencies — including credits 30-89 days past due — also moved up 3 bps to 0.39% of gross loans. Although increasing, the ratio continued to trail a national median of 0.63% (see chart).
+ Past due rates among District banks were typically led higher by C&I, and to a lesser extent, SFR and/or NFNR portfolios.
+ Within the District, delinquency ratios tended to be slightly lower among Very Small (assets below $1 billion) and Small banks (assets of $1 billion to $10 billion) compared with Mid-Sized banks (assets of $10 billion to $100 billion).

**Median Past Due Loan Rates**

*Excluding PPP loans*



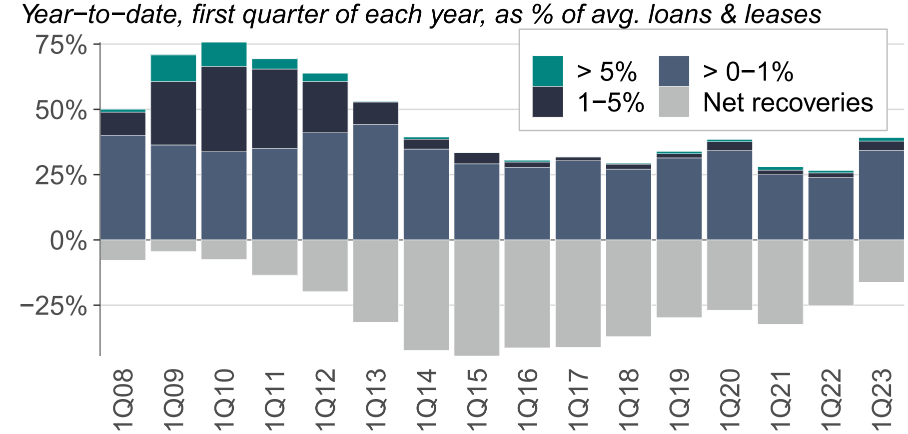

Past due includes 90+ days or nonaccrual (noncurrent) plus 30-89 days past due. Sources: Bank Call Reports/UBPRs.

## Net chargeoff activity remained limited but edged higher year-over-year.

+ Roughly 39% of District banks recorded net loan losses during 1Q23, up from 27% in the same quarter last year. Meanwhile, 16% reported net recoveries, down from 25% one year prior. Although the share incurring net chargeoffs increased, annualized loss rates generally remained below 1% (see chart).
+ Write-downs among C&I and consumer loan portfolios often drove the year-over-year increase in net chargeoffs.
+ Loan related losses would likely increase in the event of an economic slowdown. The 1Q23 CSBS Community Bank Sentiment Survey found that 64% of bankers in the "West" expected business conditions to worsen, up 3 percentage points from the prior quarter. Likewise, more than half (54%) of bankers surveyed nationwide by IntraFi Network in April expected economic conditions to weaken over the next twelve months.

**Share of Banks with Net Chargeoffs, Twelfth District**

*Year−to−date, first quarter of each year, as % of avg. loans & leases*

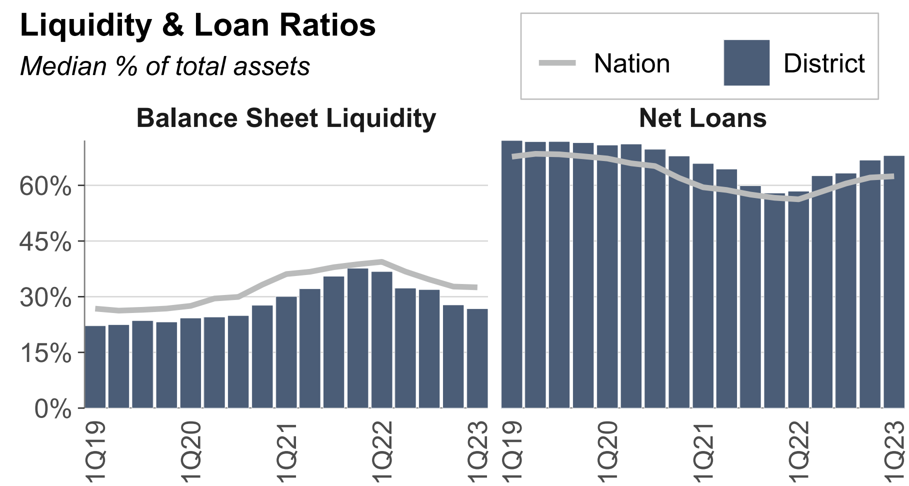



Sources: Bank Call Reports/UBPRs.

# Twelfth District Banking Conditions | Liquidity

## Banks strengthened liquid asset buffers and net unrealized bond losses moderated.

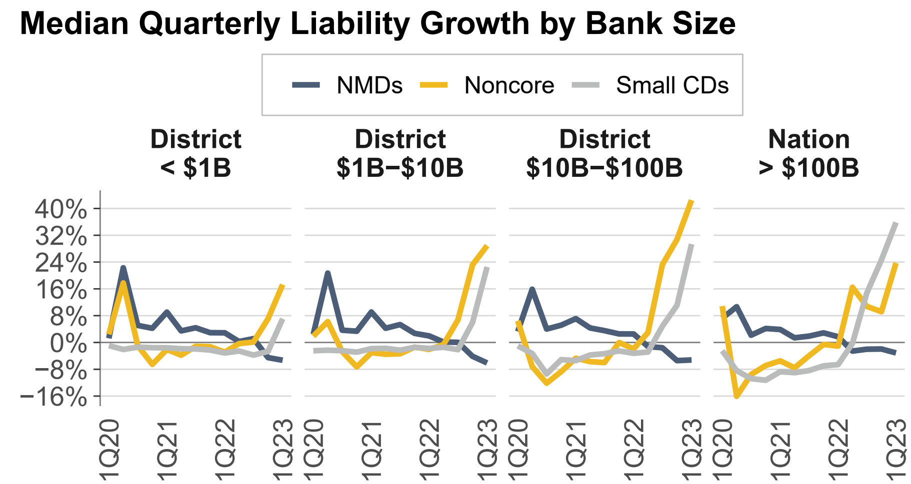
- Broadly defined, overall on-balance sheet liquidity ticked lower quarter-over-quarter (see chart).
- By March 31, liquid instruments (i.e., cash, due from accounts, Federal funds sold, and reverse repurchase agreements) represented 9.3% of assets on a median basis, up from 8.5% at year-end, but still generally below pre-pandemic levels.
- Although liquid instruments increased, securities generally eased as a share of District banks' assets, in part a function of paydowns on amortizing securities such as MBS.
- Favorably, net unrealized bond losses moderated. However, they factored into shareholder and depositor sentiment during 1Q23 and limited many banks' options for meeting funding challenges.




Balance sheet liquidity includes cash, due from accounts, fed funds sold, reverse repurchase agreements, and securities. Sources: Bank Call Reports/UBPRs.

## Nonmaturity deposit (NMD) runoff continued, prompting increased usage of noncore funding.

- Outflows of NMDs (e.g., checking, money market, and passbook deposit accounts) continued (see chart). On a median basis, NMD balances declined 5.3% across the District's banks during the quarter, led by attrition among accounts exceeding $250 thousand each.
- The share of funding from small certificates of deposit (CDs) and/or noncore liabilities increased as a result. Quarter-over-quarter, small CDs increased 29%, 23%, and 7% among Mid-Sized, Small, and Very Small District banks on a median basis, respectively. Meanwhile, the median noncore liability-to-asset ratio increased to 11% Districtwide and approached 20% among Mid-Sized District banks.
- Deposit pressures in March prompted rate promotions and a notable upward repricing of deposit products among many banks, the full effects of which may not be felt in bank earnings until 2Q23.



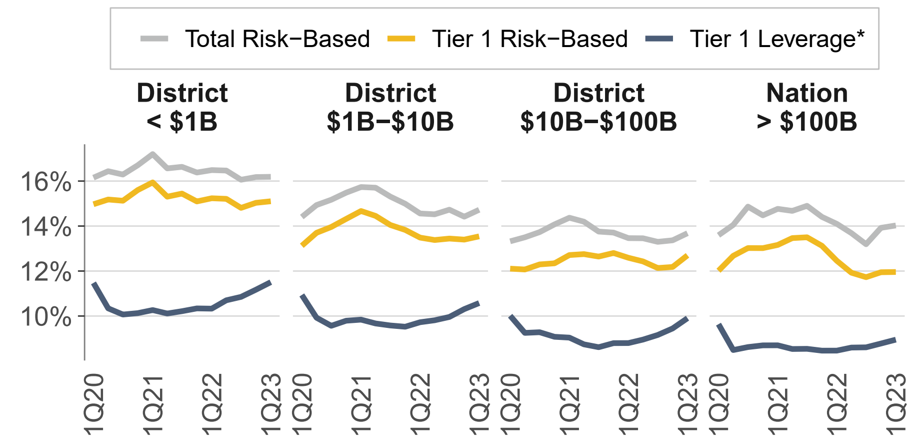

Noncore includes CDs > $250K, small brokered accounts, foreign deposits, fed funds purchased/repos, and borrowings. Sources: Bank Call Reports/UBPRs.

# Twelfth District Banking Conditions | Capital

## Regulatory capital measures generally improved, led in part by slowing growth in average and risk-weighted assets.

- District banks' median tier 1 leverage ratio was 10.72%, up 27 bps quarter-over-quarter. Median leverage ratios improved across major bank size classes (see chart). On a median basis, seasonally slower capital accretion outpaced receding average asset growth.
- Meanwhile, tier 1 and total risk-based capital (RBC) ratios each increased more than 20 bps during the quarter on a median basis. Balance sheet shifts into (lower risk-weighted) liquid instruments, in particular among Mid-Sized banks, often helped lift RBC measures.
- Accumulated other comprehensive income (loss) continued to weigh on "book" capital ratios, but to a lesser degree than in late 2022. Nearly all banks avoid AOCI inclusion in regulatory capital measures via "opt-out" provisions. Notwithstanding regulatory and accounting nuances, net unrealized bond losses influenced liquidity risks in 1Q23, especially among Mid-Sized banks.

**Median Regulatory Capital Ratios by Bank Size**



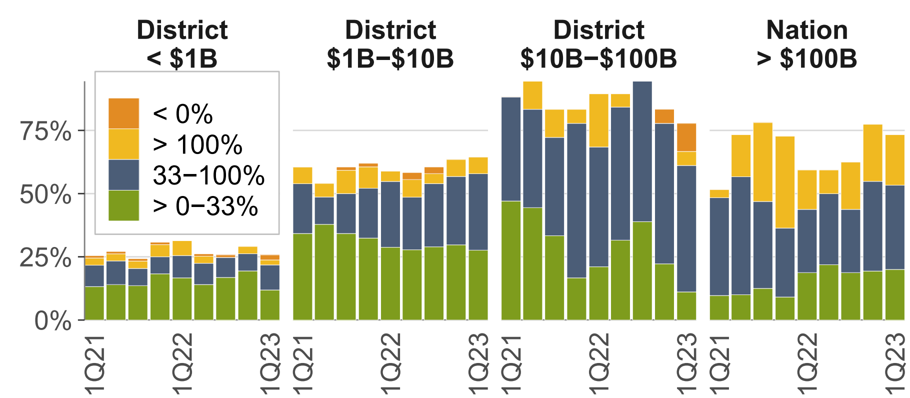

*Includes community bank leverage ratio (CBLR) reporters; CBLR banks excluded from RBC ratios beginning in 2020. Sources: Bank Call Reports/UBPRs.

## The share of non-Subchapter S banks paying dividends dipped.

- Just under half (46%) of the District's non-Subchapter S banks paid dividends during 1Q23, down from 61% in the fourth quarter – led by seasonal factors – but comparable to the same quarter last year.
- Among District banks holding less than $100 billion in assets, dividend payouts remained least common among Very Small banks and most common among Mid-Sized banks (see chart).
- For banks that are under a holding company, dividend payments upstreamed to the parent company are typically used to fund corporate dividends or repurchase shares at the consolidated firm.
- The District's 25 Subchapter S tax filing banks paid out a median 56% of profits in order to fund shareholder tax obligations atop investor returns, slightly higher than the median payout ratio of 43% among Subchapter S-filing banks nationwide.

**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 atop investor returns. Sources: 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) | |
|---|---|---|---|---|---|---|
| | *Mar-23* | *Mar-22* | *Mar-23* | *Mar-22* | *Mar-23* | *Mar-22* |
| **Alaska** | 4 (0) | 4 (0) | - | - | 1 (0) | 1 (0) |
| **Arizona** | 13 (3) | 14 (1) | - | - | 1 (0) | - |
| **California** | 117 (3) | 119 (1) | 3 (0) | 3 (0) | 9 (0) | 9 (0) |
| **Guam** | 2 (0) | 2 (0) | - | - | 1 (0) | 1 (0) |
| **Hawaii** | 3 (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) | 1 (0) | 2 (0) |
| **Oregon** | 13 (0) | 13 (0) | - | - | 2 (0) | 2 (0) |
| **Utah** | 25 (1) | 26 (1) | 15 (2) | 15 (2) | 1 (0) | 1 (0) |
| **Washington** | 33 (0) | 33 (0) | - | - | 7 (0) | 7 (0) |
| **District** | 231 (7) | 236 (4) | 23 (2) | 23 (2) | 26 (0) | 26 (0) |
| **Nation** | 4,069 (27) | 4,171 (30) | 24 (2) | 24 (2) | 575 (1) | 600 (0) |

*Based on preliminary 1Q23 data (Call Reports filed through May 11, 2023).*

- 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. 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. Also other than the table to the left, Twelfth District banking statistics include banks that are either supervised by or physically located within the Federal Reserve's Twelfth District.
- Groups by Asset Size: "Very Small", "Small", and "Mid-Sized" bank groups are based on total asset ranges of less than $1 billion, $1 to $10 billion, and $10 to $100 billion, respectively. The "Large" bank group uses banks with assets exceeding $100 billion nationwide because these banks typically operate beyond the District's geographic footprint and a larger statistical population is preferred for medians.

## 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) |
| **TE** | tax equivalent |
| **YTD** | year to date |