THE STATE OF COMMERCIAL BANKING:
2020 Market Analysis

FEATURING

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Topics

- Commercial Loan Volume
- Credit Quality
- Pricing and Fees
- Structure
- Commercial Deposits
Methodology

- The data presented in this webinar covers **commercial loans and deposits** for the 2019 calendar year.

- Primary data source: **PrecisionLender’s proprietary database**, reflecting **actual commercial relationships** (loans, deposits and other fee-based business) from **over 200 banks** in the U.S.; supplemented with **public data sources** (FDIC, Federal Reserve, etc.).

- The banks in this data set are **geographically diverse** and range in size from **community banks** to **top 10 U.S. institutions**.

- In order to provide an apples-to-apples comparison across banks, PrecisionLender has **aligned the risk rating systems** of all banks to a common scale based on Probability of Default, and has also build concordances **across products**.

- All figures (spreads, fees, risk, term, deposit rates, etc.) are **dollar-weighted**.
Commercial Loan Demand

Live Poll

How optimistic are you that your bank will achieve its loan volume goals this year?

- Highly Optimistic
- Somewhat Optimistic
- Somewhat Pessimistic
- Highly Pessimistic
Credit Conservatism

Live Poll

Do you anticipate that your bank will be more or less conservative in 2020 compared with 2019?

- More Conservative
- Less Conservative
- No Change
- It Depends on the Customer
Key Takeaways

1. Weak Outlook for Loan Demand
2. Flight to Quality / Market Bifurcation
3. Quality of Borrowers and Structures Is Under Pressure
4. Risk/Return Is Steepening
5. Deposit Gathering Is Key
2019: From Optimism to Concern

*Source: Federal Reserve H15 Release*
C&I Loan Growth Plummets

C&I Loan Growth Rates: 2018-2019

*Source: Federal Reserve H8 Release*
C&I Loan Growth Plummets

*Source: Federal Reserve H8 Release
Low Expectations for 2020 Commercial Loan Demand

**Key Economic Indicators Associated With Loan Demand**

**GDP Growth**

**Unemployment Rate**

*Source: Federal Reserve FOMC (Federal Open Market Committee) Projections*
Low Expectations for 2020 Commercial Loan Demand

*CSource: Federal Reserve Senior Loan Officer Opinion Survey on Bank Lending Practices.*
Low Expectations for 2020 Commercial Loan Demand

*Source: Federal Reserve Senior Loan Officer Opinion Survey on Bank Lending Practices.*
Where is the Volume Coming From?

A Considerable Portion of Loan Activity Stems from Renewals

- Renewals
- Originations

Greater Loyalty to Incumbent Bank on Smaller Accounts

**Source: PrecisionLender.**
Increased Emphasis on Adjustable Rate Pricing

Adjustable Rate Incidence Trends Higher

*Source: PrecisionLender.*
Signs of Credit Stress?

C&I Delinquencies Tick Higher but Continue to Drop for CRE

*Source: Federal Reserve*
Signs of Credit Stress?

Credit Downgrades Outpace Upgrades

*Source: PrecisionLender.*
Signs of Credit Stress?

LOC Utilization Rates are Down Slightly

*Source: PrecisionLender.
Structural Trends: Increasing LOC Commitment Limits

2019 Renewal Line Changes

- Commitment reduction: 32%
  Balance reduction: 21%
- Line reduction: 12%
- Commitment change: 0%
  Balance reduction: 1%
- No change in commitment: 57%
- Line increase: 31%
  Balance increase: 37%

*Source: PrecisionLender.*
Structural Trends: Collateral is Still Key

Unsecured Incidence Edges Higher, But Collateral Remains Largely Non-Negotiable

2018
- Unsecured: 7%
- Secured: 93%

2019
- Unsecured: 10%
- Secured: 90%

*Source: PrecisionLender.*
Structural Trends: Concessions for Larger Customers

Banks Offer Generous LTVs on Larger Credits, Pull Back on Smaller Deals

*Source: PrecisionLender.*
Structural Trends: Concessions for Larger Customers

Terms Extended on Credits to Larger Borrowers

Average Term
Aggregate Market

Average Change: 0.4 years

Change in Term (years)

Average Change in Term
By Size

Deal Amount ($)

*Source: PrecisionLender.
Charge-Offs Are Low, But Recovery Rates Have Dropped

*Source: FDIC. Data reflects all U.S. commercial banks. Figures aggregated based on call report filings.
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Credit Execs Expect Tighter Standards

Q4 2019 Brought a Shift in Credit Standards

*Source: FDIC. Data reflects all U.S. commercial banks. Figures aggregated based on call report filings.
Market Bifurcation Evident in Pricing Trends

*Source: PrecisionLender*
Market Bifurcation Evident in Pricing Trends

*Source: PrecisionLender

[Graph showing improved discipline in pricing for risk]
Fixed Rates Fell, But FTP Fell More

Spreads Contract After Widening Most of the Year

- **< $100K**
- **$100K - $250K**
- **$250K - $500K**
- **$500K - $1MM**

*Source: PrecisionLender*
Despite Pockets of Improvement, NIM Still Trending Lower

*Source: FDIC. Data reflects all U.S. commercial banks. Figures aggregated based on call report filings.*
Good News on the Fee Front

Fee Penetration Rates Continue to Rise

*Source: PrecisionLender*
A Pessimistic Pricing Outlook

Bankers Expect Pricing Pressure to Persist

*Source: Federal Reserve Senior Loan Officer Opinion Survey on Bank Lending Practices.*
Commercial Deposits and Ancillary Business

Live Poll

In 2020, do you expect your bank to step-up its focus on winning commercial deposits and/or other cross-sell?

- Increase Focus on Winning Commercial Deposits
- Increase Focus on Cross-Sell / Ancillary Fee-Based Business
- Increase Focus on Both Deposits and Cross-Sell
- No Change
A Shift Away from Interest-Free DDAs

Less Capital in Interest-Free DDA Accounts

*Source: PrecisionLender
Competitive Rates Offered to Attract Deposits

Negotiated Commercial Deposit Rates Rise Sharply with Size

*Source: PrecisionLender*
Self-Funding: Merits and Challenges

Deposit/Loan Ratios Drop as Borrower Size Rises

*Source: PrecisionLender
Similar “Markets” Not Necessarily in Close Proximity

Aggregate Deposits vs. Average
Selected Cities

San Antonio, TX
Miami, FL
Jacksonville, FL
Redding, CA
Philadelphia, PA
Omaha, NE
Denver, CO
New York, NY
Washington, DC
Brooklyn, NY
West Palm Beach, FL
Anchorage, AK
Austin, TX
San Francisco, CA
Richmond, VA
Tampa, FL
Charlottesville, VA
Lancaster, PA
Lees Summit, MO
Orlando, FL
Fort Lauderdale, FL
Memphis, TN
Fort Worth, TX
Boulder, CO
Virginia Beach, VA
Kansas City, MO
Knoxville, TN

% of Nationwide Average for Similar Customers

*Source: PrecisionLender
Concluding Thoughts

• Commercial banking market starting to prepare for the next downturn, albeit slowly

• Credit execs believe it’s time to tighten the reins on credit

• Sales execs are struggling to achieve growth goals and maintain NIM given (1) weak loan demand; (2) intense non-bank competition; (3) declining rates; and (4) narrowing margins

• Bankers are pulling out all the stops to win business, but are being selective – giving up price and structure for the right customer – resulting in a bifurcation of the market

• Across the portfolio, bankers are pursuing deposit opportunities to lower funding costs and increase NIM, while concurrently stepping up efforts to win lucrative cross-sell to strengthen relationship profitability
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May 6-8, 2020
Austin, Texas
Pricing Competitively With Market Insights

FEATURED

Tim Shanahan
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PrecisionLender, a Q2 Company

Thursday, February 13th @1PM EST