BANKING & FINANCE

Banking Conditions, Regulatory Updates Discussed in New "ViewPoint"

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Allow me to introduce myself - I'm Cynthia Goodwin, vice president in Supervision, Regulation, and Credit, filling in for Mike Johnson. Mike has accepted an interim position at the Board of Governors. While Mike is away, I will be leading the Division and communicating with you via ViewPoint!

This edition of ViewPoint includes our regular feature, State of the District. We are also preparing articles on the Economic Growth, Regulatory Relief, and Consumer Protection Act, an update on fintech activity, and a look at conditions in commercial real estate. First, as always, we review the State of the District.

State of the District

First quarter financial results revealed continued stable performance for banks in the District. Recent increases in interest rates boosted earnings for many institutions. The median return on average assets (ROAA) for community banks was 1.05 percent. The aggregate ROAA has been above 1 percent in four of the last five quarters. The median tier 1 common equity ratio was just below 15 percent, recovering from the decline in the prior quarter, which was caused by recognition of the impact of recent changes in tax laws. Despite the length of the recovery and some indications of looser underwriting practices in recent quarters, asset quality remained stable. In the first quarter, the charge-off ratio fell to a three-year low. Median liquidity on hand increased slightly to 18.6 percent. Since the fed funds rate began to rise, the deposit mix has shifted very little. As of the first quarter, nonmaturity deposits were still growing.

Although conditions in the District appear stable, certain trends bear watching. As interest rates continue to rise, "sticky" deposits may become mobile, forcing banks to raise rates to retain funds. In the first quarter of 2018, median asset growth at community banks slowed to the lowest level in nearly three years, due largely to a decline in loan growth. If the slowdown in lending continues and the cost of deposits rises, the net interest margin could narrow quickly. On the credit side, recent data reported by Fitch indicate that default rates on subprime auto loans exceed levels seen in the financial crisis. As interest rates adjust, more borrowers may have trouble meeting their obligations. According to creditcard.com, in June 2018, average credit card interest rates reached the highest level in more than ten years. Banks must be prepared to respond quickly to changes in interest rate risk and continue to focus on sound banking practices.

Regulatory Update

Economic Growth, Regulatory Relief, and Consumer Protection Act

The big news affecting supervision and regulation this quarter is the passage of the Economic Growth, Regulatory Relief, and Consumer Protection Act on May 24, 2018. The act raises the threshold for many Dodd-Frank regulatory requirements and mandates a reduction in the regulatory burden for smaller firms. Developing rules and adapting supervisory programs to meet the requirements of the new law are priorities for the banking agencies. We expect to hear more shortly regarding implementation plans.

In the interim, please submit questions regarding the act to EGRRCPA@frb.gov. The Board of Governors will be responding to issues raised. Additional information on the Act will be provided in an article next month. Stay tuned for more details!

CRE appraisal requirement threshold

On April 2, 2018, the regulatory agencies approved a final rule increasing the commercial real estate (CRE) threshold for which an appraisal is required from $250,000 to $500,000. An evaluation will be required for exempt transactions, including a market value estimate but will not require compliance with uniform standards of practice or the use of a licensed appraiser. The request for comment proposed a threshold of $400,000, but research indicated that an increase to $500,000 would materially reduce the regulatory burden without threatening safety and soundness.

CECL regulatory capital transition

On April 17, 2018, the agencies proposed a revision to regulatory capital rules to address the regulatory capital impact of the new Current Expected Credit Losses (CECL) methodology. The proposed rule would provide an optional three-year phase-in period. The proposal would revise the Board's regulatory capital rules and other rules to take into consideration the new accounting standard.

Save the Date—Viewpoint Live

Please join us for the next Viewpoint Live on Thursday, October 4, 2018, at 1 p.m. In addition to our regular review of banking conditions, we will discuss developments in fintech. Remember to check back here for the registration link for this special event and to read the articles that will be published next quarter. In the meantime, check out the *Economy Matters* podcast episode on CRE disrupters, featuring our Risk Analysis Unit.

As always, I welcome your comments or questions. Please share your feedback with me at ViewPoint@atl.frb.org.

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