The IRA Bank Book

Q2 2024 Industry Review & Outlook

ISBN 978-0-692-09756-4
www.theinstitutionalriskanalyst.com

Review & Outlook

- US bank industry income was up slightly in 1Q 2024, with lower net interest income again but a rebound in non-interest revenue. A $20 billion uptick in non-interest income for CCAR banks (SIFMA) after the huge decline in Q4 2024 was very welcome indeed and pushed results higher overall. Total interest expense rose 3x faster than interest income, resulting in a modest decline in net interest income across the industry.
- Credit continued to be a mixed bag with commercial loans, autos and credit cards leading the way higher for defaults, but residential mortgages still lingering around zero net loss due to strong home prices. That said, most of the banks we track in the WGA Bank Top 100 indices are showing higher levels of non-performing assets, even if provisions for loss were actually down sequentially. Look for higher provisions in Q2.
- With loan growth flopping around either side of 1% for all banks, balance sheet expansion has been a function of increases in available for sale securities for the first time in several years. A focus on raising liquidity, cutting costs and remediating delinquent commercial credits means that the industry will be distracted and thus unlikely to deliver strong revenue or earnings growth in 2024.

WGA Bank Top 25 Index (WBXXVW)

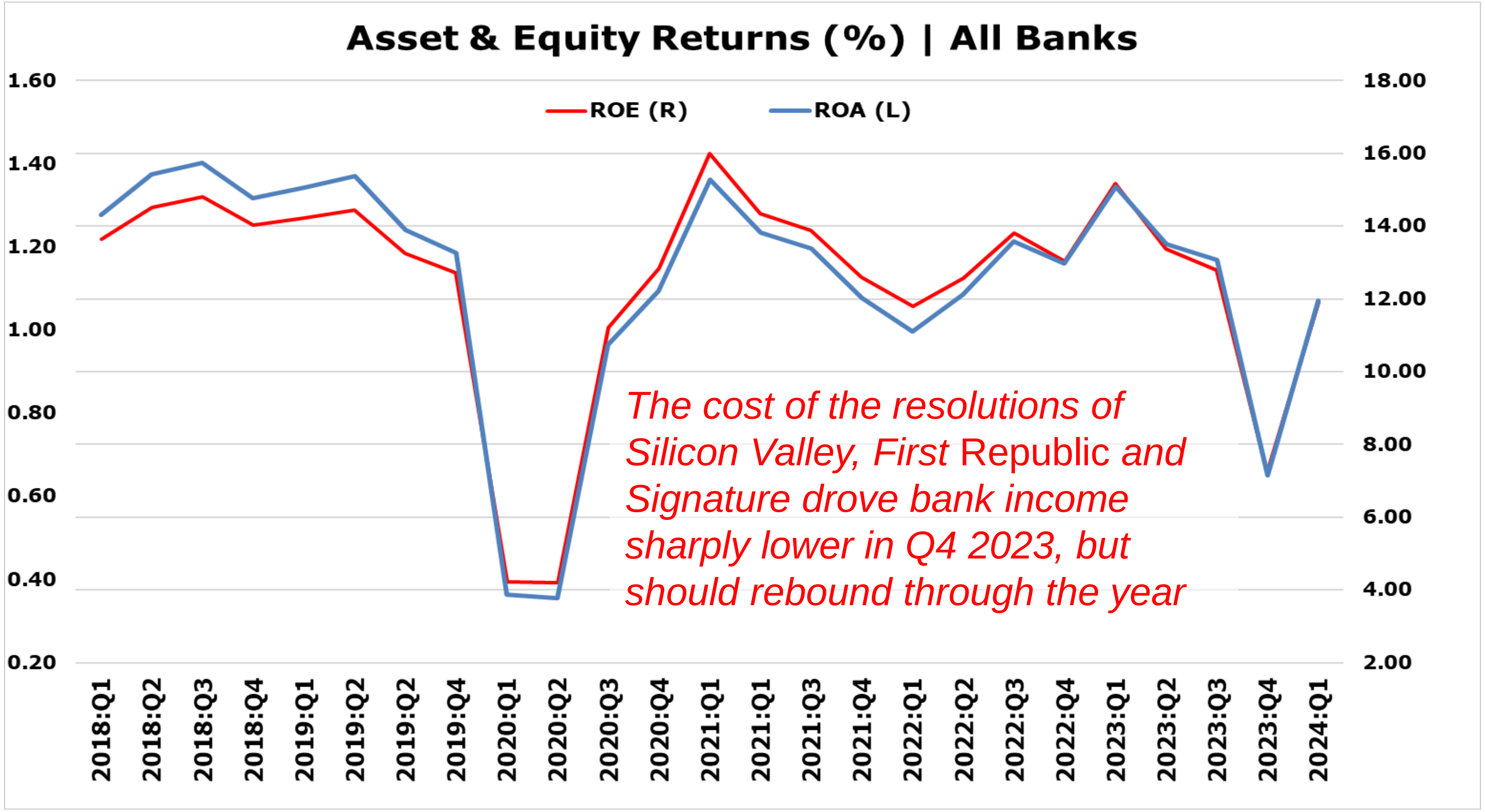
https://www.theinstitutionalriskanalyst.com/indices

WGA BANK TOP 100
Q2 2024

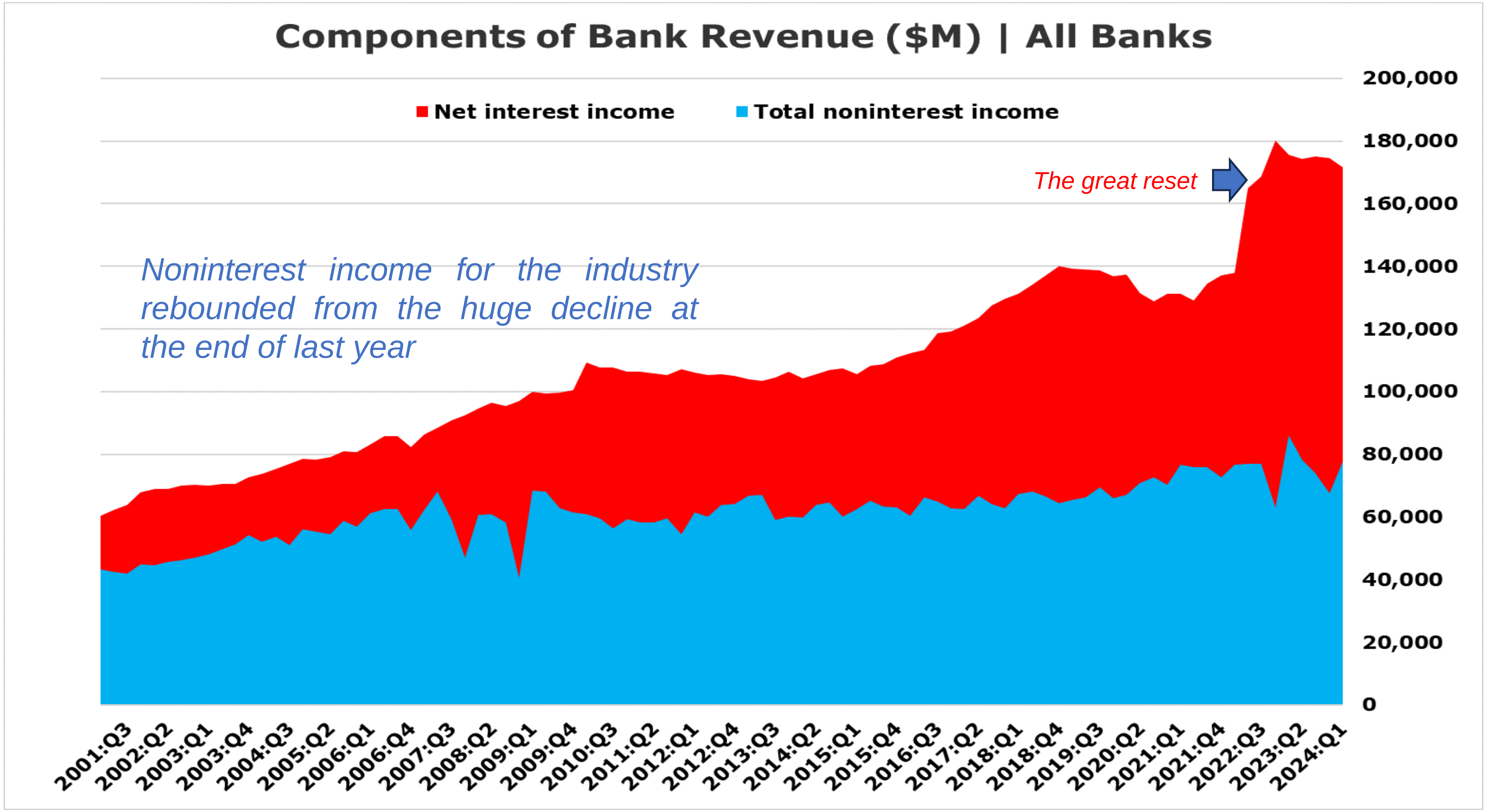
Ticker	Rank	Ticker	Rank	Ticker	Rank	Ticker	Rank	Ticker	Rank
DFS	1	MTB	26	SSB	51	LOB	76	BRKL	101
JPM	2	MS	27	BMO	52	BUSE	77	SASR	102
SYF	3	BAC	28	WBS	53	EBC	78	PPBI	103
FCNCA	4	HBAN	29	CUBI	54	INDB	79	IBTX	104
EWBC	5	GS	30	FCF	55	UCBI	80	NYCB	105
AXP	6	OFG	31	PB	56	ASB	81	FFWM	106
SCHW	7	SF	32	FULT	57	VBTX	82		
IBOC	8	MBIN	33	TRMK	58	TCBI	83		
FITB	9	UMBF	34	FRME	59	BKU	84		
AMP	10	FHN	35	KEY	60	VLY	85		
FBP	11	USB	36	SOFI	61	NWBI	86		
CFR	12	BOKF	37	ABCB	62	PFS	87		
RJF	13	CMA	38	CBU	63	STEL	88		
WFC	14	BPOP	39	NBTB	64	HOPE	89		
FFIN	15	SNV	40	STT	65	LBAI	90		
AX	16	BK	41	GBCI	66	SBCF	91		
BANF	17	ONB	42	C	67	WSBC	92		
SFBS	18	ZION	43	BANR	68	EGBN	93		
RF	19	CVBF	44	CFG	69	HTLF	94		
HOMB	20	WAL	45	AUB	70	DCOM	95		
COF	21	NTRS	46	FBK	71	RNST	96		
WTFC	22	FHB	47	COLB	72	HTH	97		
PNC	23	BOH	48	TFC	73	OCFC	98		
TD	24	WSFS	49	FIBK	74	BHLB	99		
OZK	25	ALLY	50	WAFD	75	SFNC	100		

Q1 2024

- Because the US banking sector reported higher earnings in Q1 2024, investors may think incorrectly that the difficult times are behind us. Many bank stocks hit new 12-month highs during the quarter as non-interest revenue rebounded as is usually the case in the first quarter of the year. **JPMorgan (JPM)** peaked on March 17th a tad under $205 per share and well-above 2x book value.
- "A large decline in noninterest expense (down $22.5 billion, or 13.3 percent) was the primary driver of the increase in net income. A decline in the expense related to the special assessment accounted for more than half of the decline in noninterest expense," reports the FDIC. Credit cards and commercial loans showed elevated levels of delinquency, particularly for larger banks.
- Loss severities on CRE exposures continue to climb and <u>we have included several new charts for owner occupied and non-owner occupied assets</u>. The noncurrent rate for non-owner occupied CRE loans of 1.59 percent in first quarter 2024 was at its highest level since fourth quarter 2013, driven by office portfolios at the largest banks, says FDIC. We expect loss rates on CRE and cards to continue rising throughout the year.



Source: FDIC/WGA LLC


Components of Bank Revenue ($M) | All Banks
Net interest income
Total noninterest income
The great reset
Noninterest income for the industry rebounded from the huge decline at the end of last year
200,000
180,000
160,000
140,000
120,000
100,000
80,000
60,000
40,000
20,000
0
2001:Q3
2002:Q2
2003:Q1
2003:Q4
2004:Q3
2005:Q2
2006:Q1
2006:Q4
2007:Q3
2008:Q2
2009:Q1
2009:Q4
2010:Q3
2011:Q2
2012:Q1
2012:Q4
2013:Q3
2014:Q2
2015:Q1
2015:Q4
2016:Q3
2017:Q2
2018:Q1
2018:Q4
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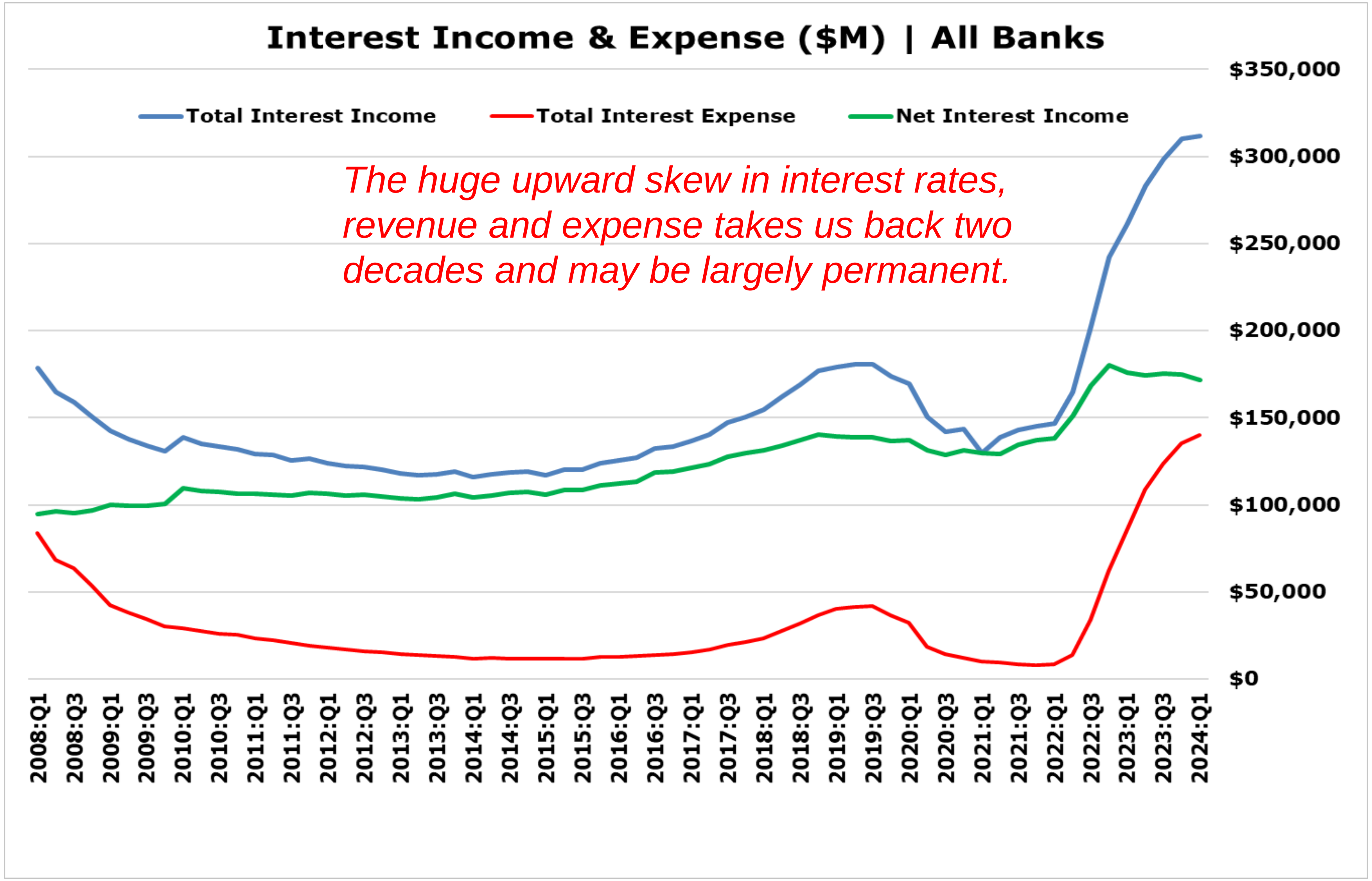
2020:Q2
2021:Q1
2021:Q4
2022:Q3
2023:Q2
2024:Q1

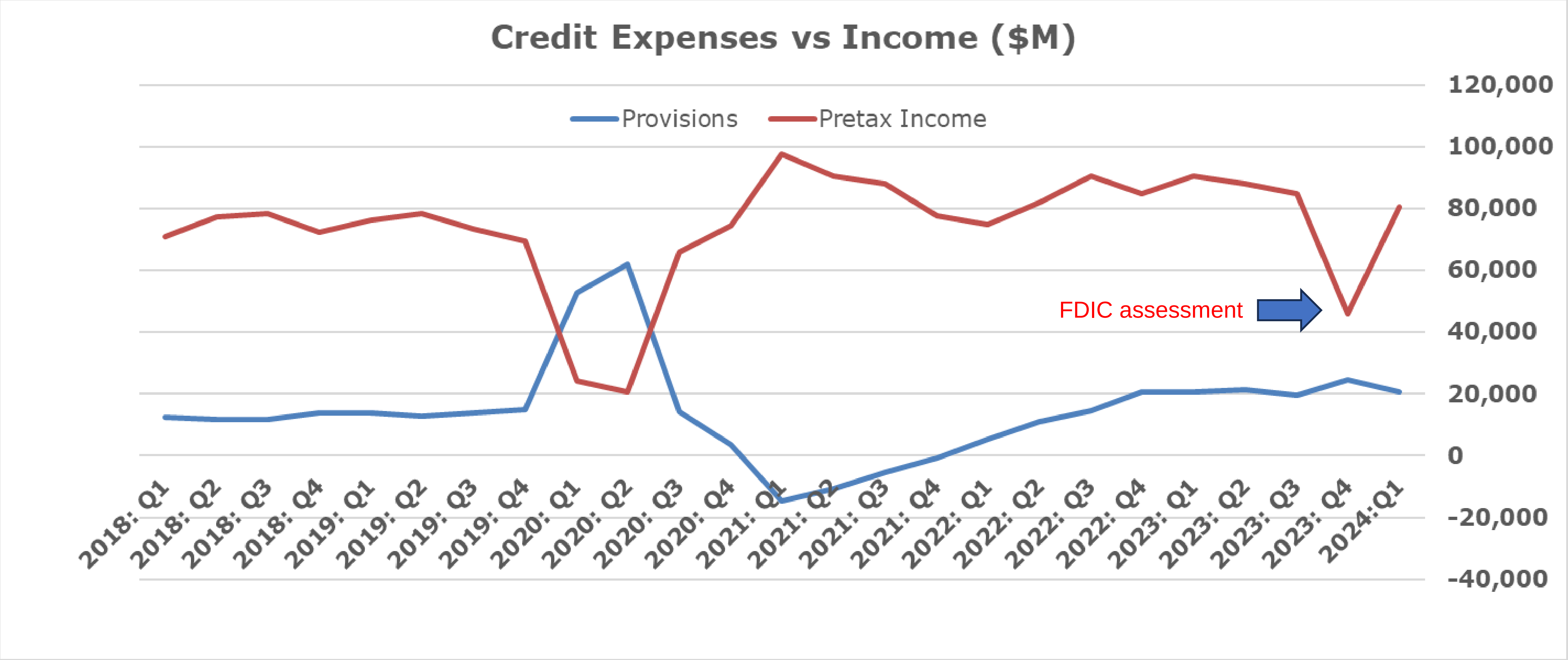
Source: FDIC



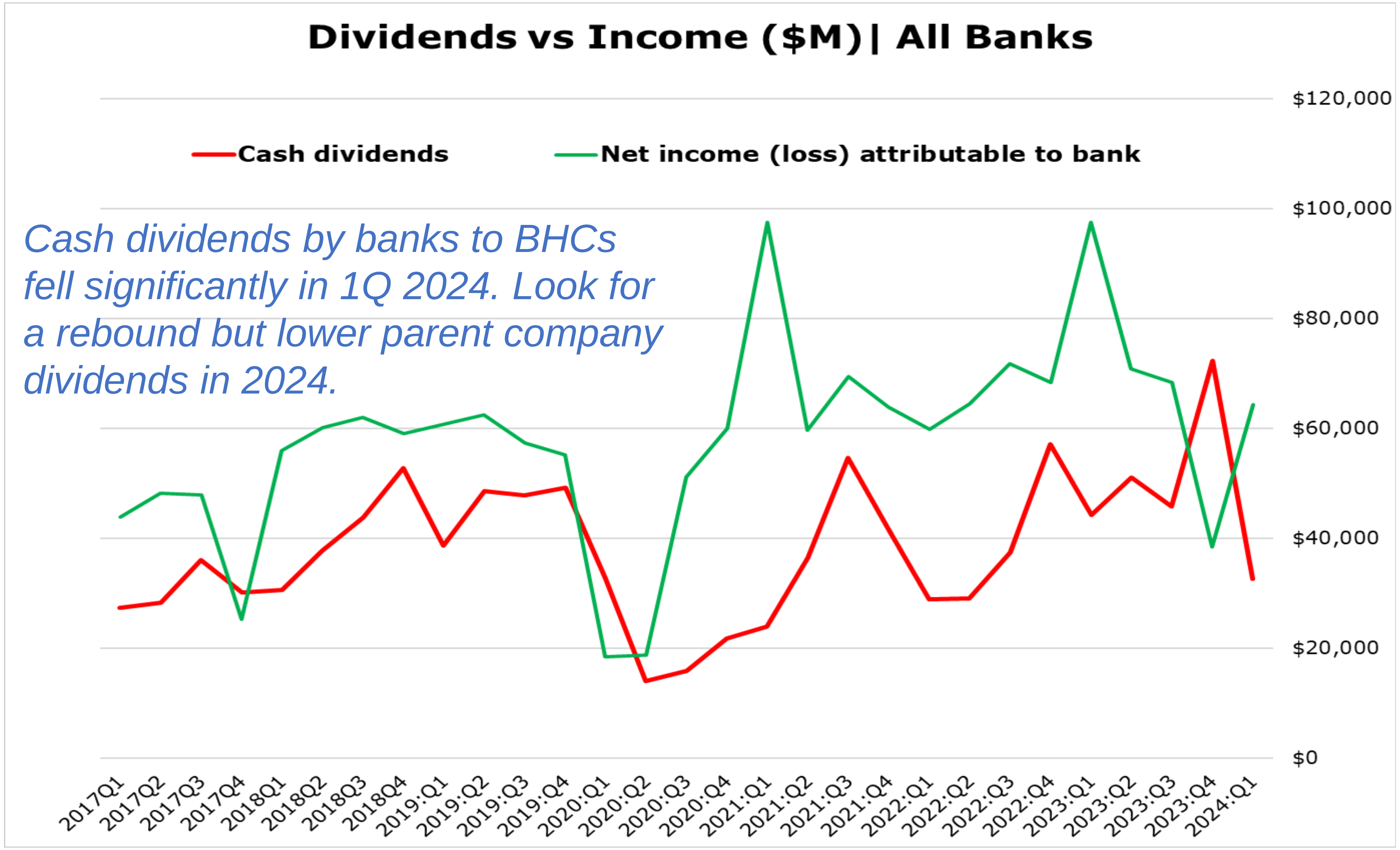
Interest Income & Expense ($M) | All Banks
Total Interest Income
Total Interest Expense
Net Interest Income
The huge upward skew in interest rates, revenue and expense takes us back two decades and may be largely permanent.
$350,000
$300,000
$250,000
$200,000
$150,000
$100,000
$50,000
$0
2008:Q1
2008:Q3
2009:Q1
2009:Q3
2010:Q1
2010:Q3
2011:Q1
2011:Q3
2012:Q1
2012:Q3
2013:Q1
2013:Q3
2014:Q1
2014:Q3
2015:Q1
2015:Q3
2016:Q1
2016:Q3
2017:Q1
2017:Q3
2018:Q1
2018:Q3
2019:Q1
2019:Q3
2020:Q1
2020:Q3
2021:Q1
2021:Q3
2022:Q1
2022:Q3
2023:Q1
2023:Q3
2024:Q1

Source: FDIC

Provision for future credit losses declined modestly in Q1 2024 as pre-tax income rose dramatically



Source: FDIC


Dividends vs Income ($M)| All Banks
Cash dividends
Net income (loss) attributable to bank
Cash dividends by banks to BHCs fell significantly in 1Q 2024. Look for a rebound but lower parent company dividends in 2024.
$120,000
$100,000
$80,000
$60,000
$40,000
$20,000
$0
2017Q1
2017Q2
2017Q3
2017Q4
2018Q1
2018Q2
2018Q3
2018Q4
2019:Q1
2019:Q2
2019:Q3
2019:Q4
2020:Q1
2020:Q2
2020:Q3
2020:Q4
2021:Q1
2021:Q2
2021:Q3
2021:Q4
2022:Q1
2022:Q2
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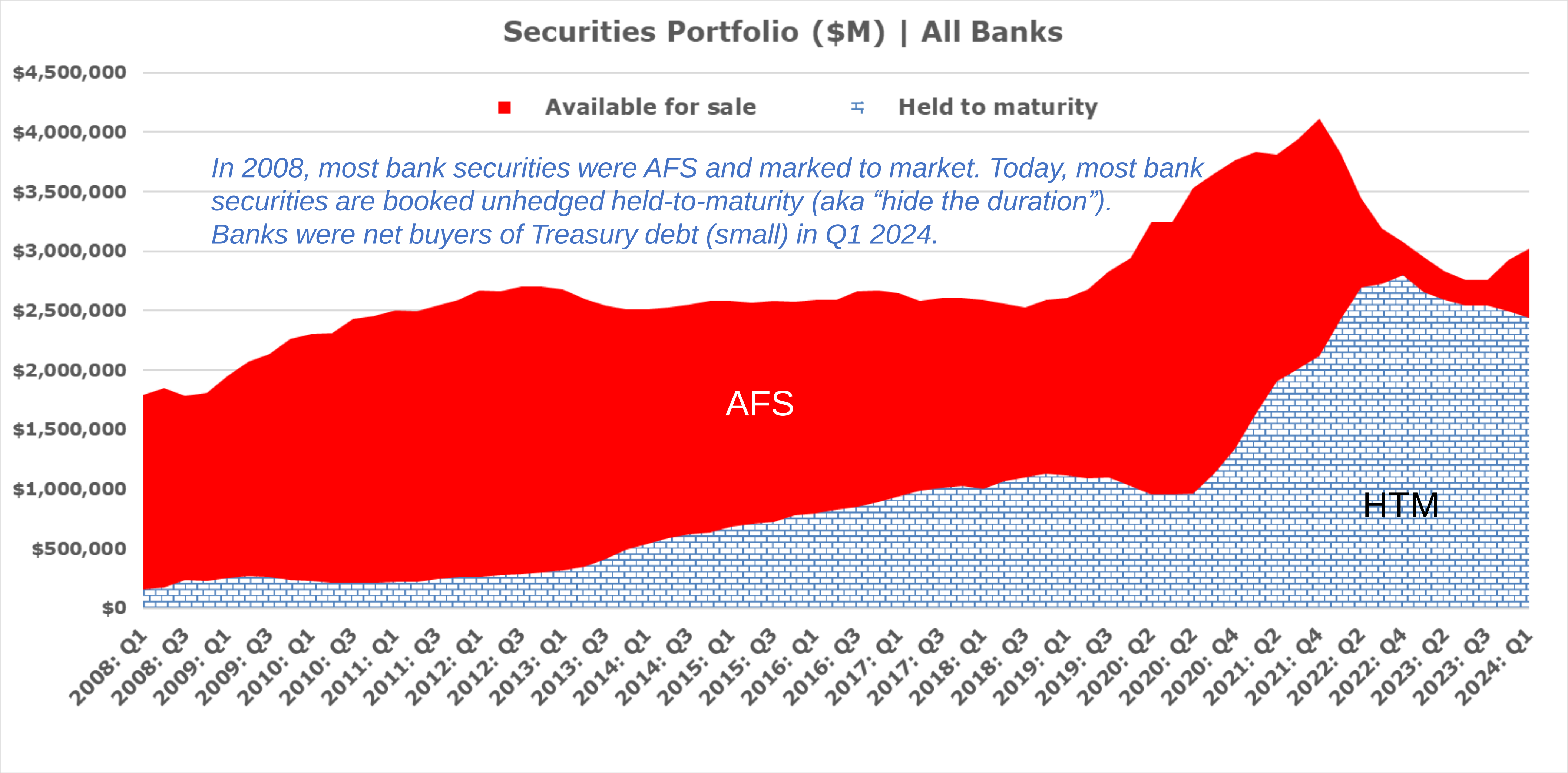
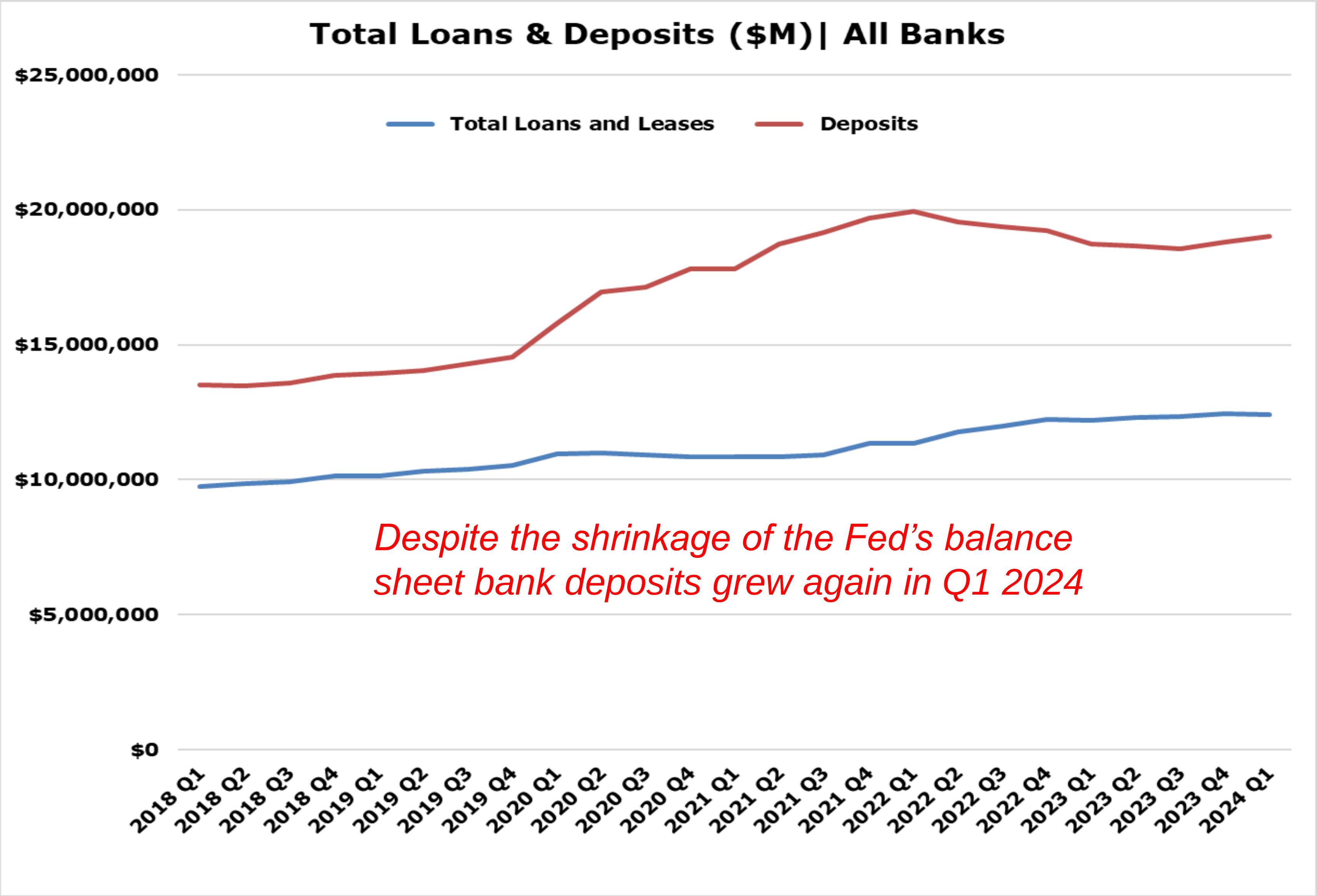
2022:Q4
2023:Q1
2023:Q2
2023:Q3
2023:Q4
2024:Q1

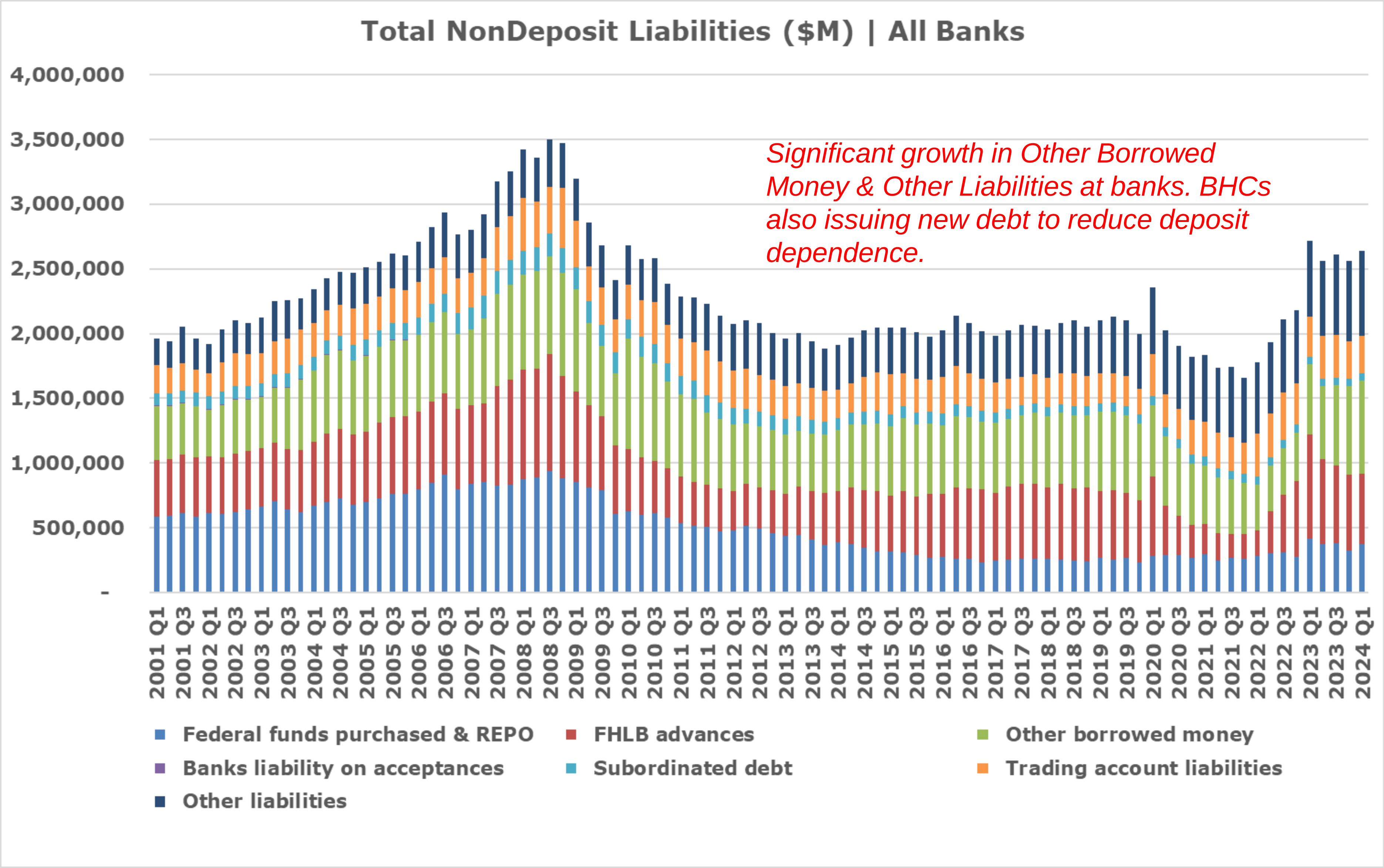
Source: FDIC


Securities Portfolio ($M) | All Banks
Available for sale
Held to maturity
$4,500,000
$4,000,000
$3,500,000
$3,000,000
$2,500,000
$2,000,000
$1,500,000
$1,000,000
$500,000
$0
In 2008, most bank securities were AFS and marked to market. Today, most bank securities are booked unhedged held-to-maturity (aka "hide the duration").
Banks were net buyers of Treasury debt (small) in Q1 2024.
AFS
HTM
2008: Q1
2008: Q3
2009: Q1
2009: Q3
2010: Q1
2010: Q3
2011: Q1
2011: Q3
2012: Q1
2012: Q3
2013: Q1
2013: Q3
2014: Q1
2014: Q3
2015: Q1
2015: Q3
2016: Q1
2016: Q3
2017: Q1
2017: Q3
2018: Q1
2018: Q3
2019: Q1
2019: Q3
2020: Q2
2020: Q2
2020: Q4
2021: Q2
2021: Q4
2022: Q2
2022: Q4
2023: Q2
2023: Q3
2024: Q1

Source: FDIC


Total Loans & Deposits ($M)| All Banks
Total Loans and Leases
Deposits
$25,000,000
$20,000,000
$15,000,000
$10,000,000
$5,000,000
$0
2018 Q1
2018 Q2
2018 Q3
2018 Q4
2019 Q1
2019 Q2
2019 Q3
2019 Q4
2020 Q1
2020 Q2
2020 Q3
2020 Q4
2021 Q1
2021 Q2
2021 Q3
2021 Q4
2022 Q1
2022 Q2
2022 Q3
2022 Q4
2023 Q1
2023 Q2
2023 Q3
2023 Q4
2024 Q1
Despite the shrinkage of the Fed's balance sheet bank deposits grew again in Q1 2024

Source: FDIC


Total NonDeposit Liabilities ($M) | All Banks
4,000,000
3,500,000
3,000,000
2,500,000
2,000,000
1,500,000
1,000,000
500,000
-
2001 Q1
2001 Q3
2002 Q1
2002 Q3
2003 Q1
2003 Q3
2004 Q1
2004 Q3
2005 Q1
2005 Q3
2006 Q1
2006 Q3
2007 Q1
2007 Q3
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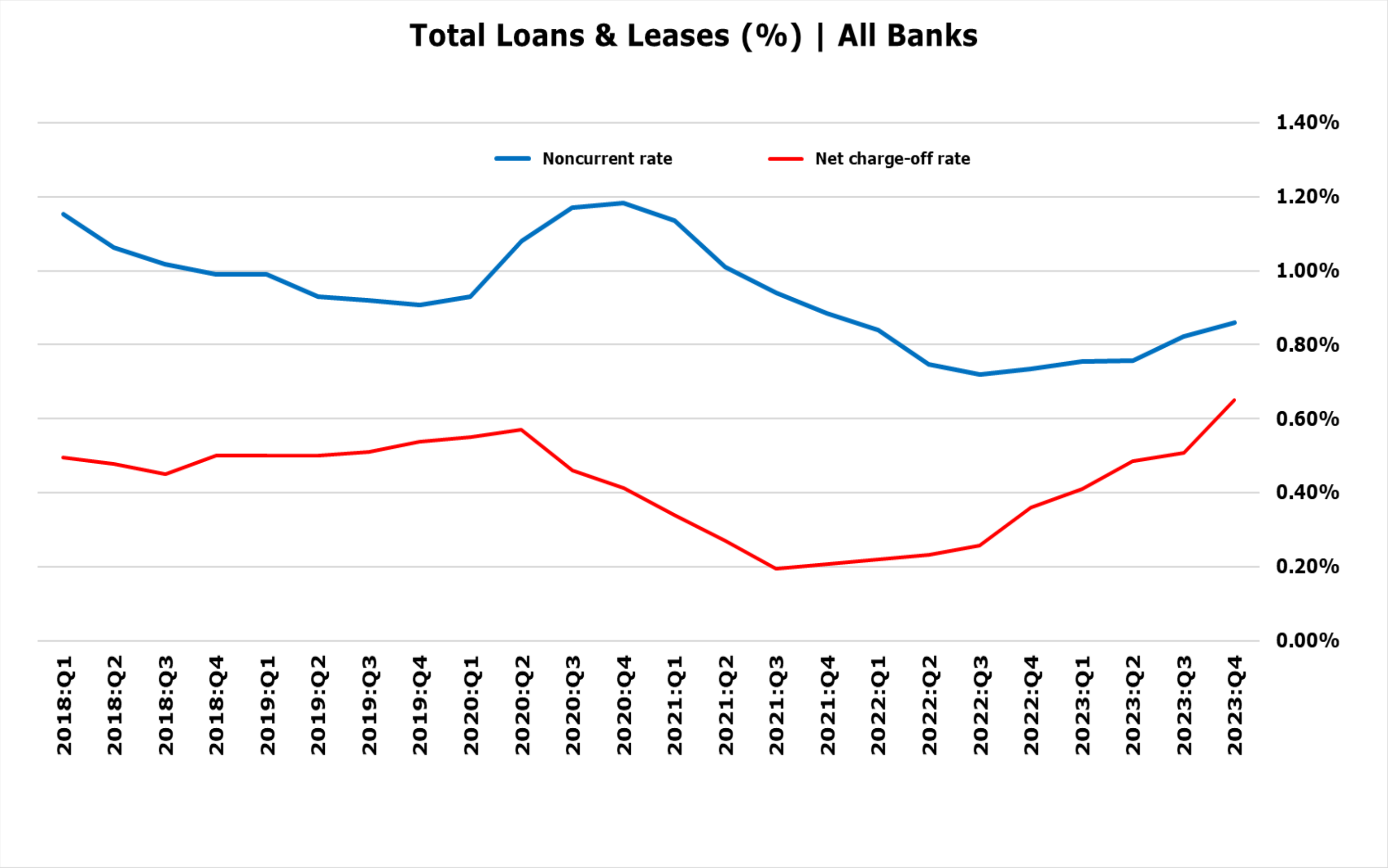
2018 Q3
2019 Q1
2019 Q3
2020 Q1
2020 Q3
2021 Q1
2021 Q3
2022 Q1
2022 Q3
2023 Q1
2023 Q3
2024 Q1
Federal funds purchased & REPO
FHLB advances
Other borrowed money
Banks liability on acceptances
Subordinated debt
Trading account liabilities
Other liabilities
Significant growth in Other Borrowed Money & Other Liabilities at banks. BHCs also issuing new debt to reduce deposit dependence.

Credit Charts

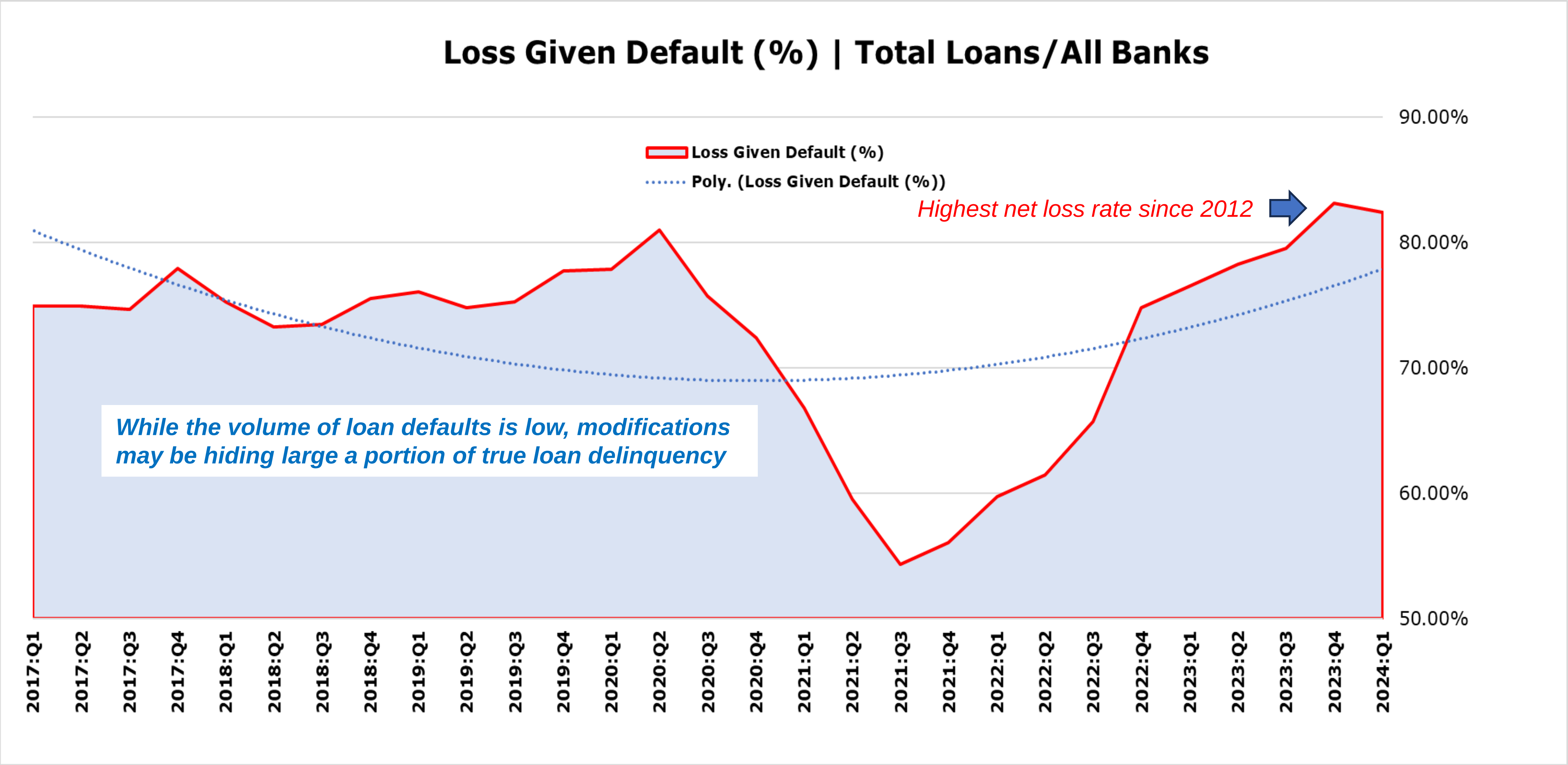
FDIC SCHEDULE RC-C DEFINITIONS

Total Loans & Leases

- Delinquency levels for the $12.4 trillion in bank portfolio loans rose again in Q1 2024, quickening the rate of increase from 2023. Banks continue to modify and extend loans at a brisk pace, partially masking true level of consumer *and* commercial delinquency by as much as half.
- The noncurrent rate for non-owner occupied CRE loans of 1.59 percent in Q1 2024 was at its highest level since 2013, driven by office portfolios at the largest banks. As shown in the following slides, loss severities for bank loans generally continue to increase.

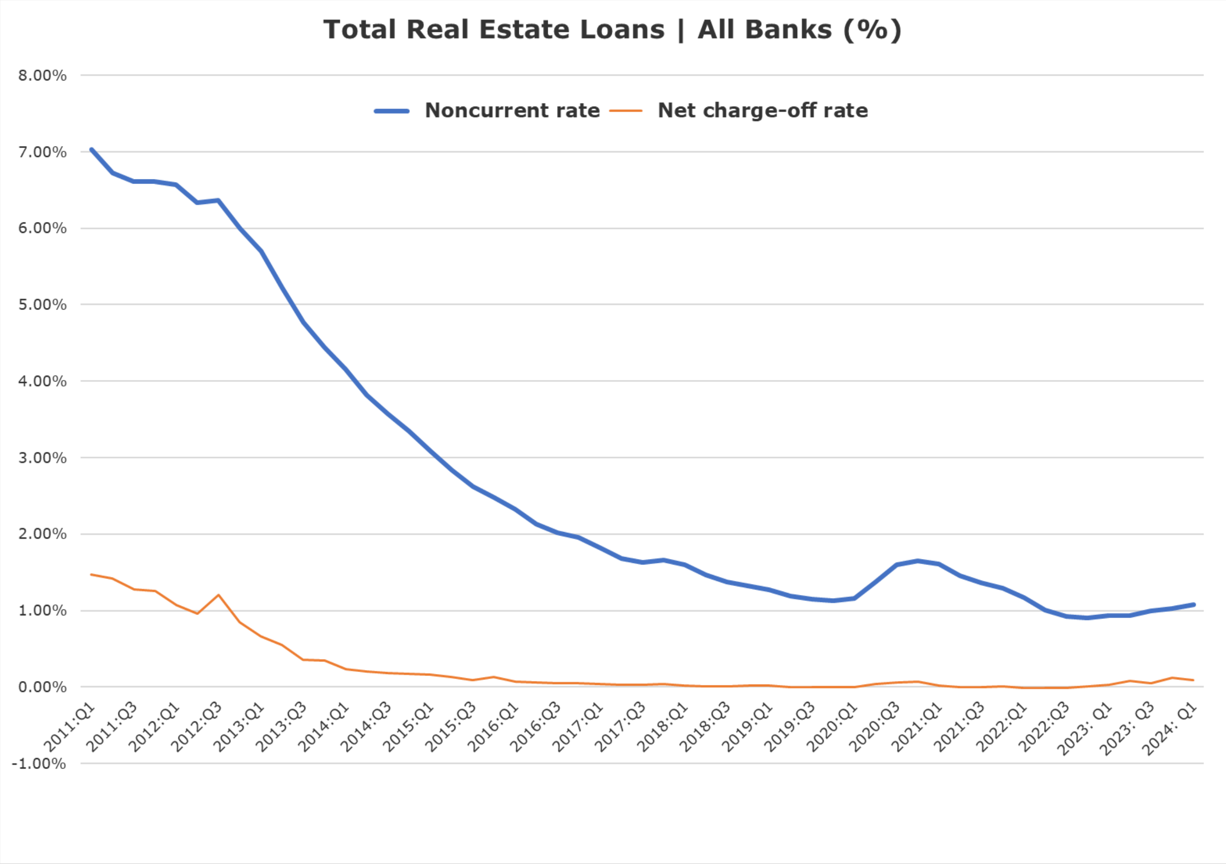


Source: FDIC

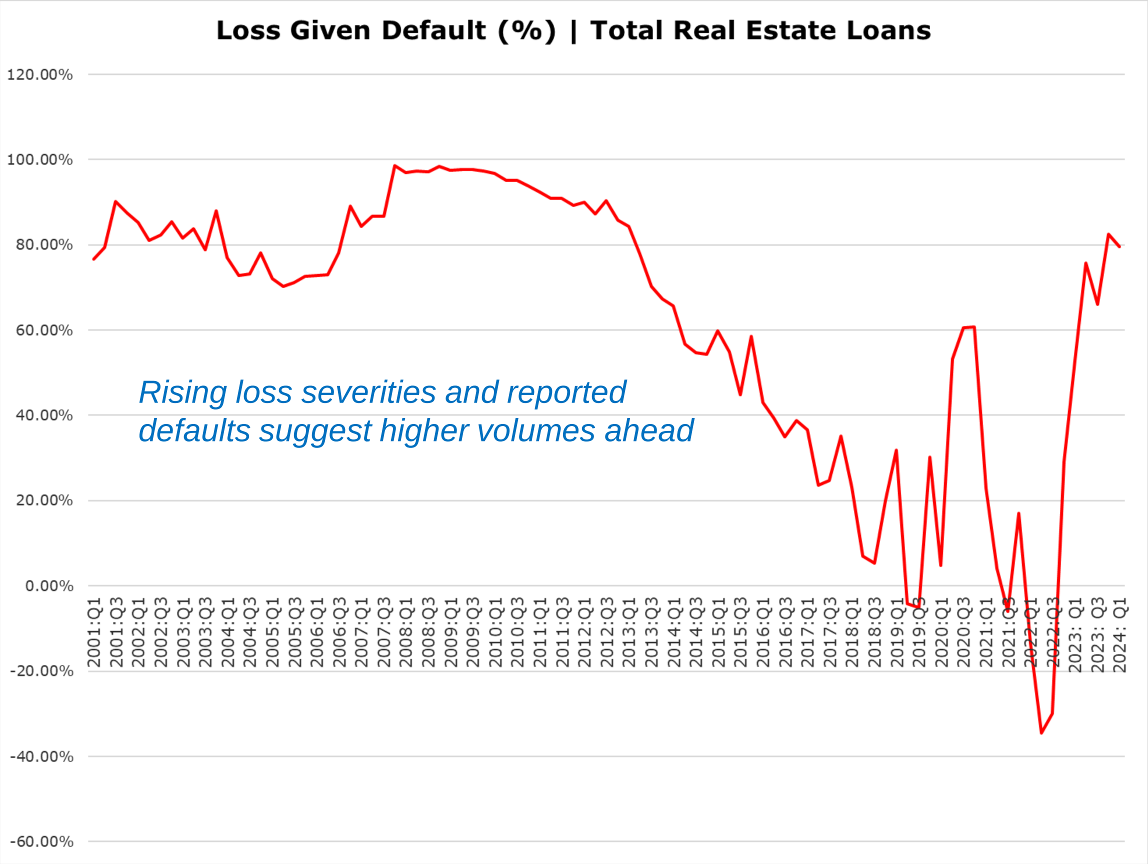

Loss Given Default (%) | Total Loans/All Banks
Loss Given Default (%)
Poly. (Loss Given Default (%))
Highest net loss rate since 2012
While the volume of loan defaults is low, modifications may be hiding large a portion of true loan delinquency
90.00%
80.00%
70.00%
60.00%
50.00%
2017:Q1
2017:Q2
2017:Q3
2017:Q4
2018:Q1
2018:Q2
2018:Q3
2018:Q4
2019:Q1
2019:Q2
2019:Q3
2019:Q4
2020:Q1
2020:Q2
2020:Q3
2020:Q4
2021:Q1
2021:Q2
2021:Q3
2021:Q4
2022:Q1
2022:Q2
2022:Q3
2022:Q4
2023:Q1
2023:Q2
2023:Q3
2023:Q4
2024:Q1

Source: FDIC

CRE Losses Pull Up Severity for All Real Estate Loans

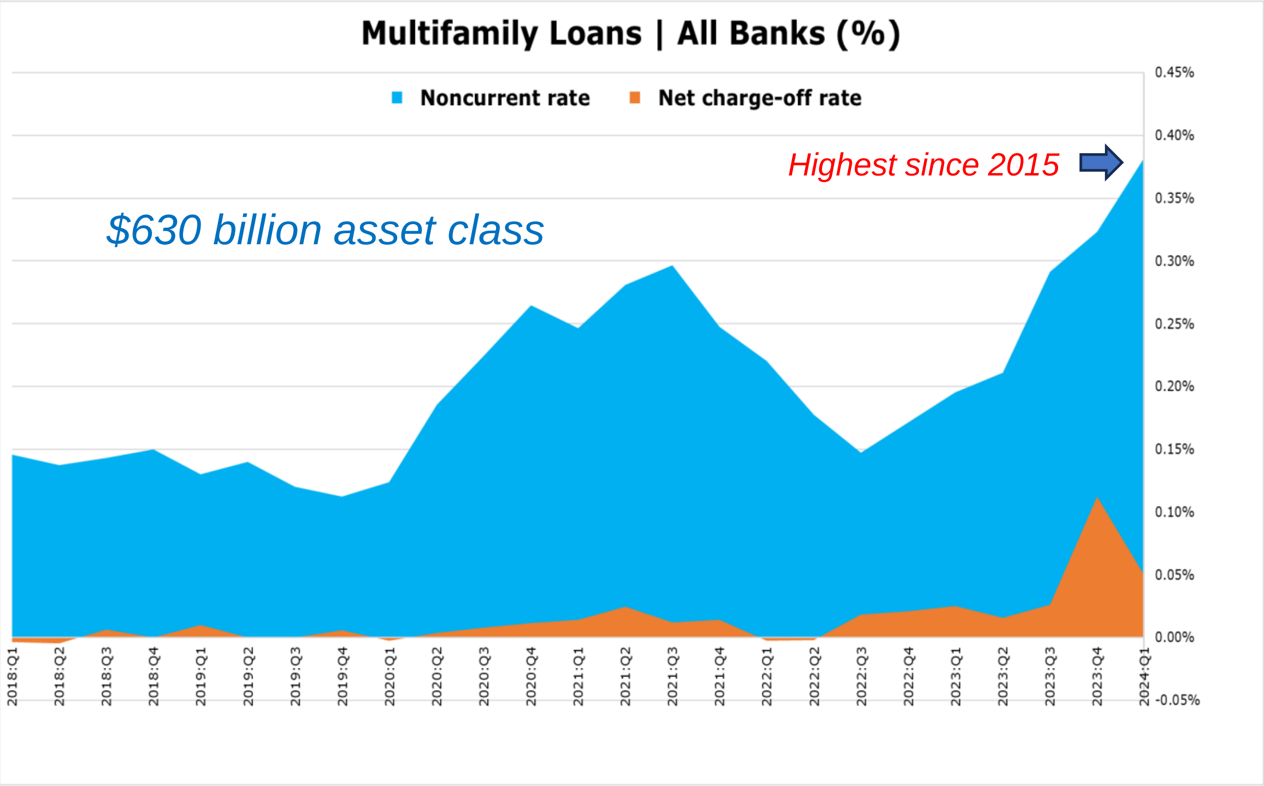


Source: FDIC

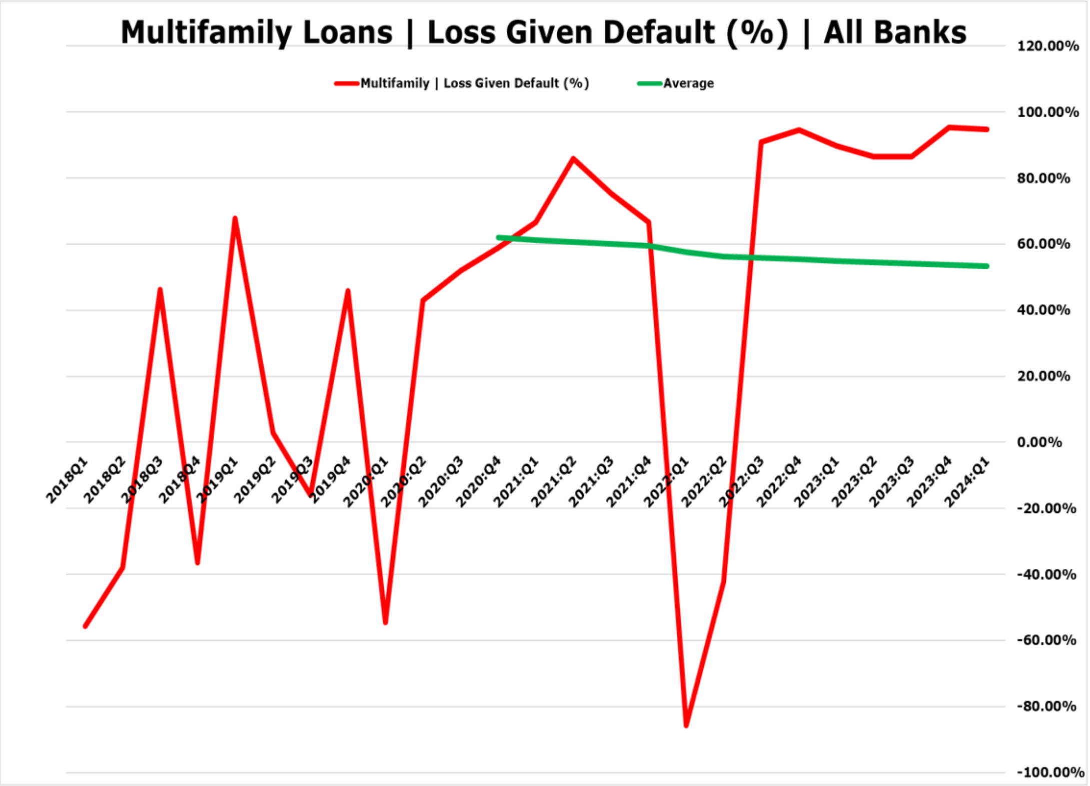


Source: FDIC/WGA LLC

Multifamily Assets Lead Loss Severity on CRE

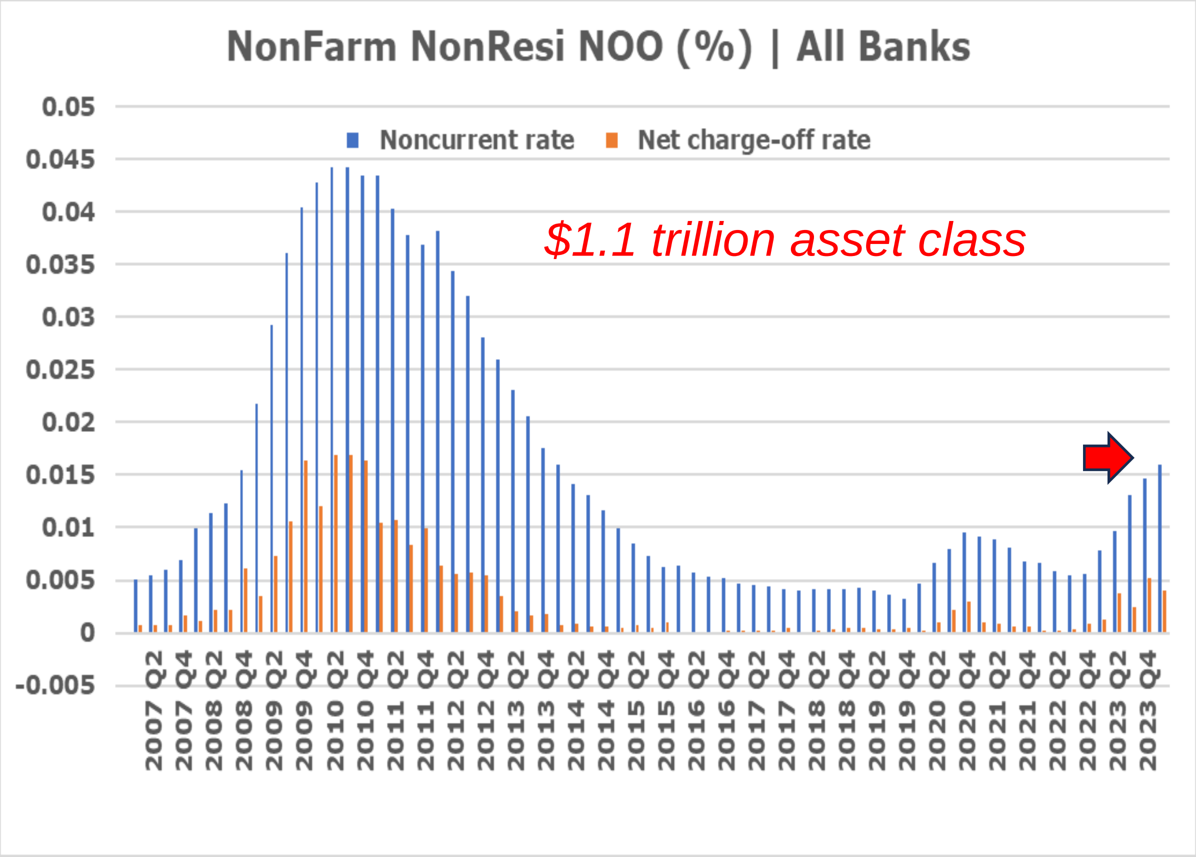


Source: FDIC



Source: FDIC/WGA LLC

NonFarm, NonResi NOO CRE Loss Severity Rising Sharply



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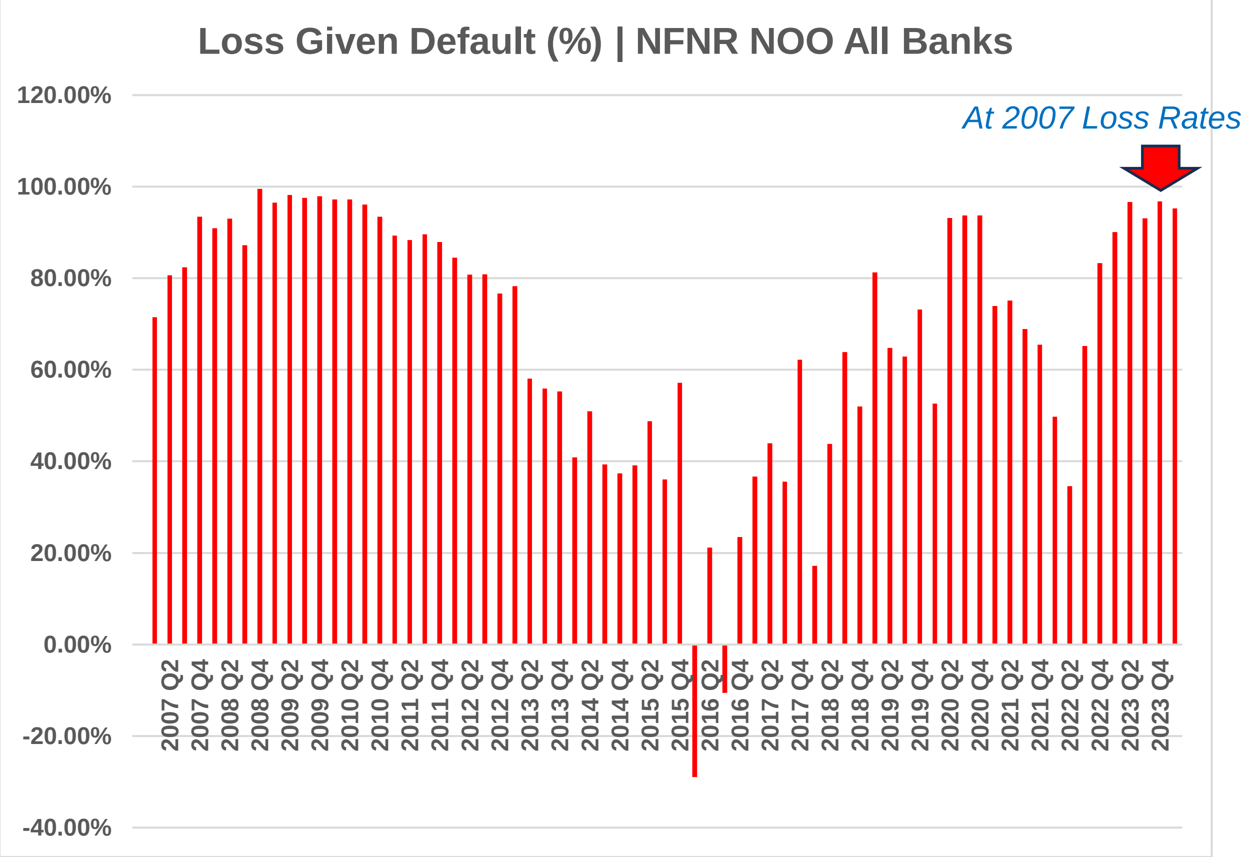
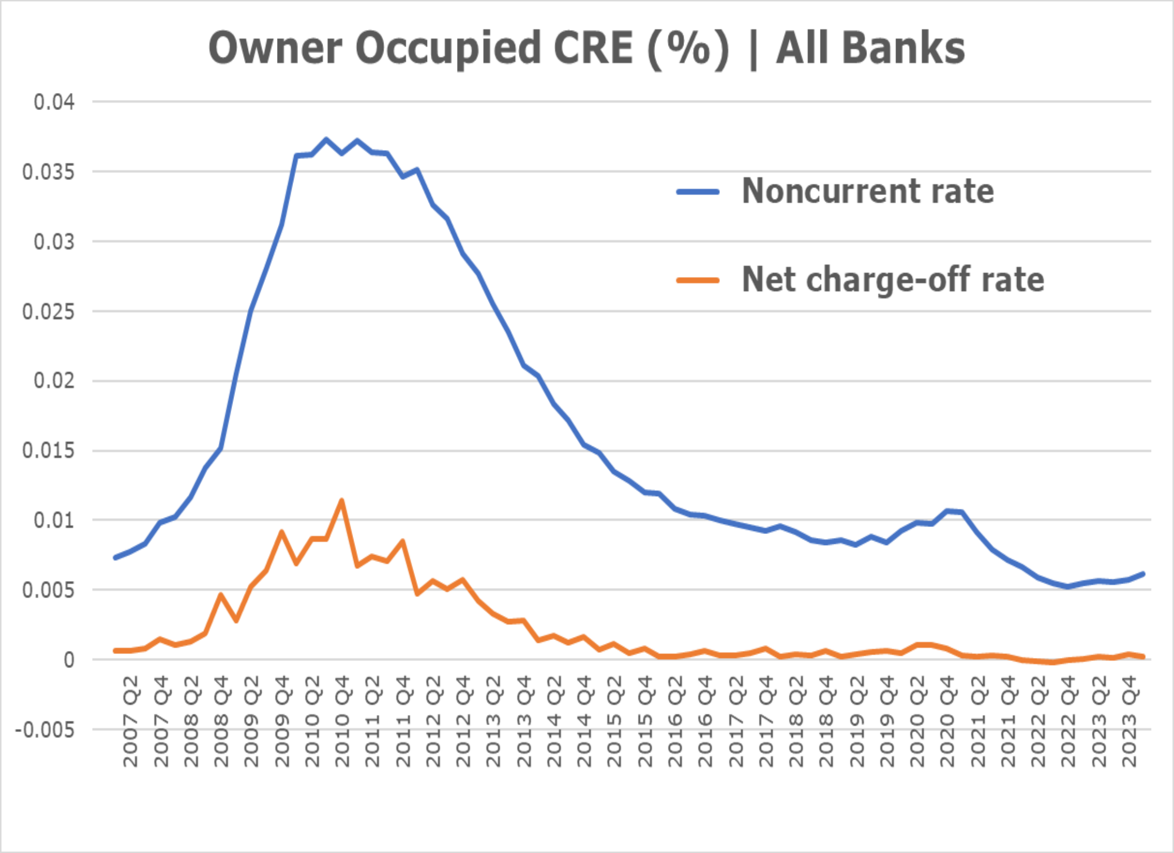
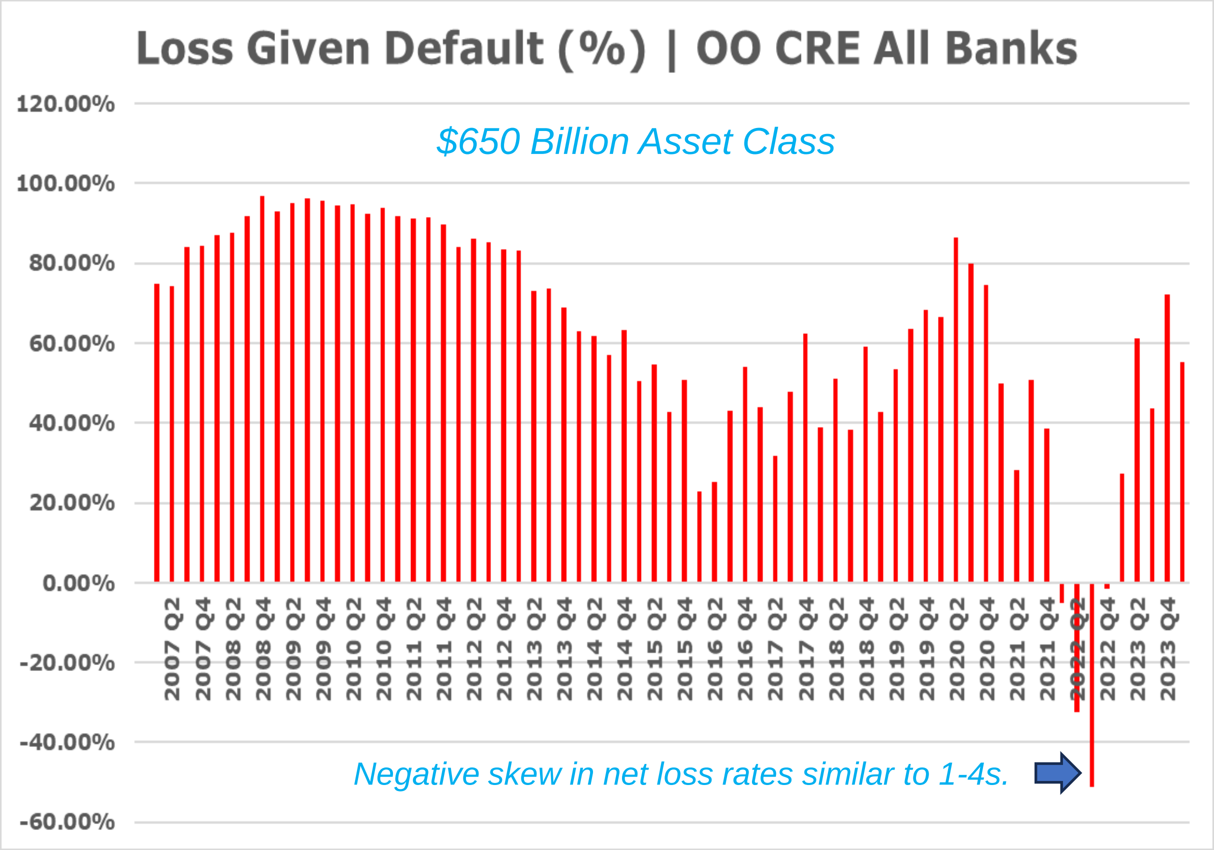


Source: FDIC/WGA LLC

Owner Occupied CRE Loss Rates Normalizing



Source: FDIC

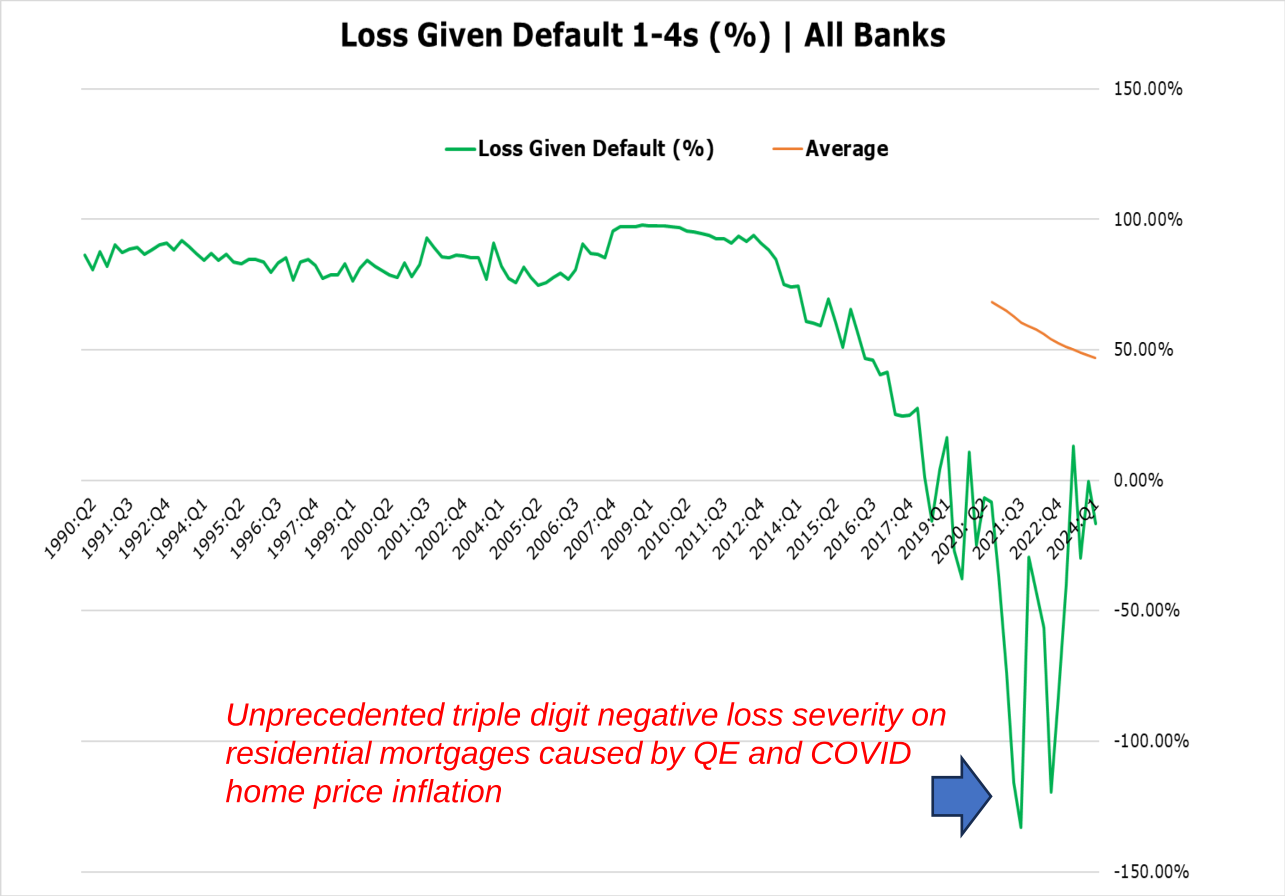


Source: FDIC/WGA LLC

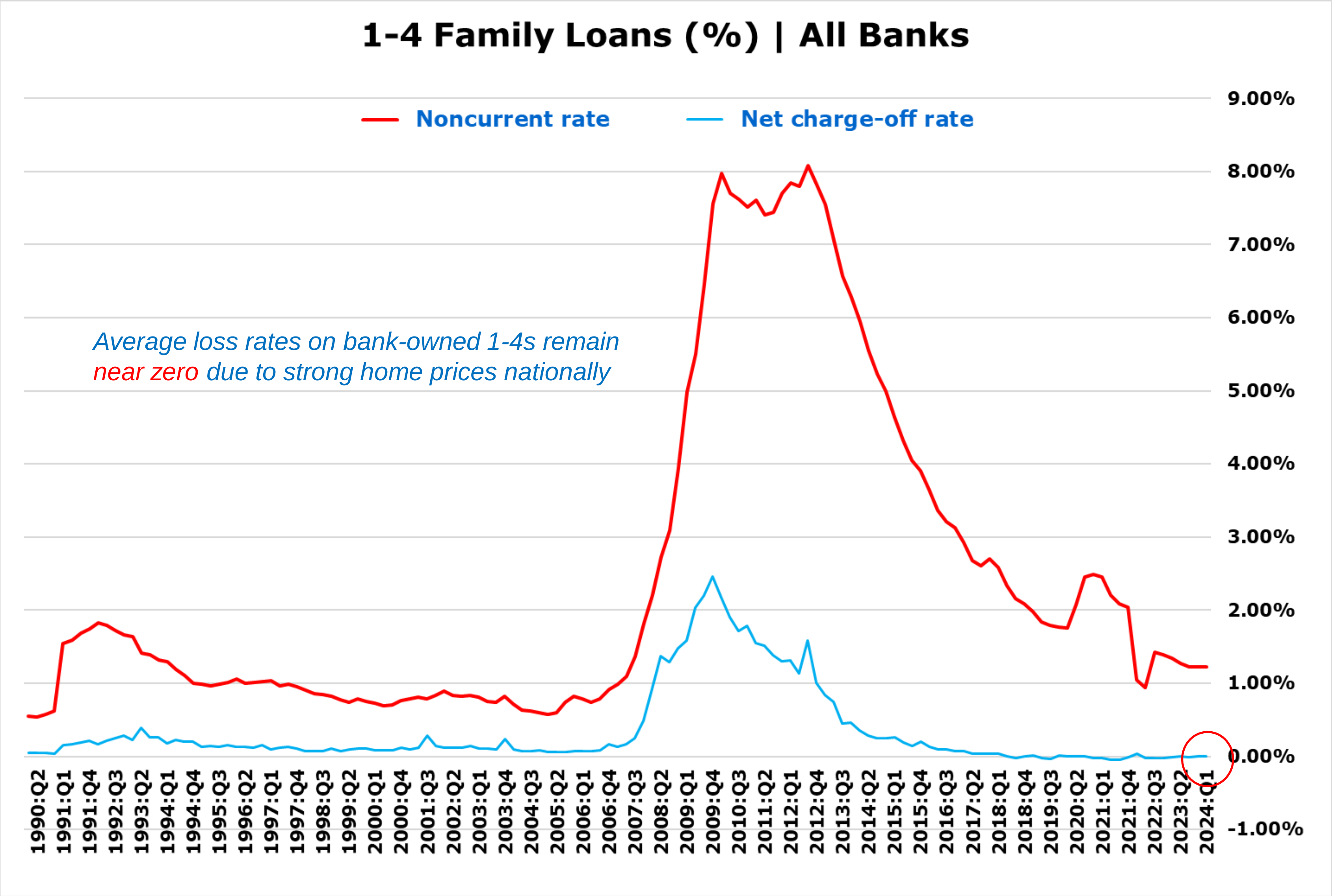
Residential Mortgage Loans

- Negative loss rates on bank-owned 1-4 family residential loans skewed downward in Q3 and Q4 2023. The continued increase in home prices illustrates how difficult it will be to see relief for consumers in terms of affordability.

- LGD for 1-4s moved into positive territory in Q2 after touching record negative levels but went negative again in Q1 2024. Forty-year average LGD stood below 50% in Q4 2023. Loss rates after 2008 were over 100% of loan balance.



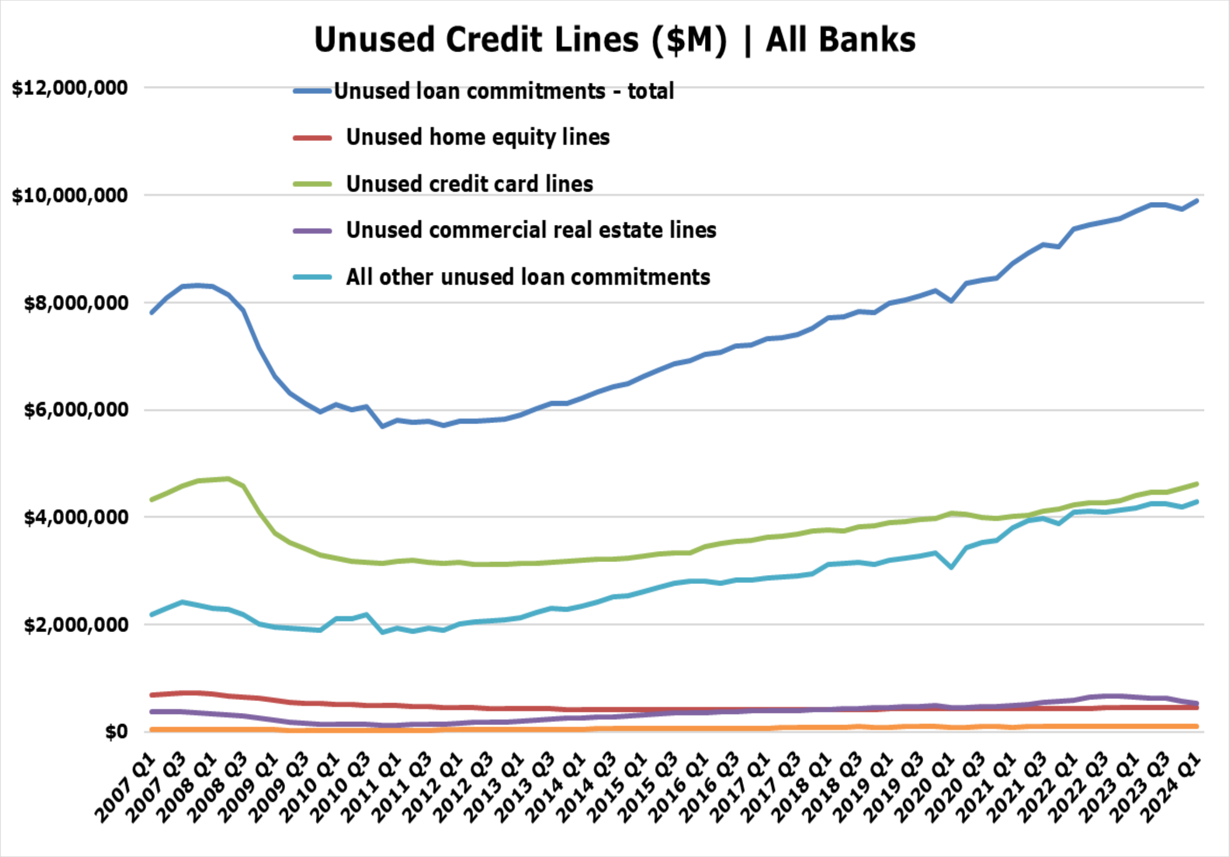
Source: FDIC/ WGA LLC



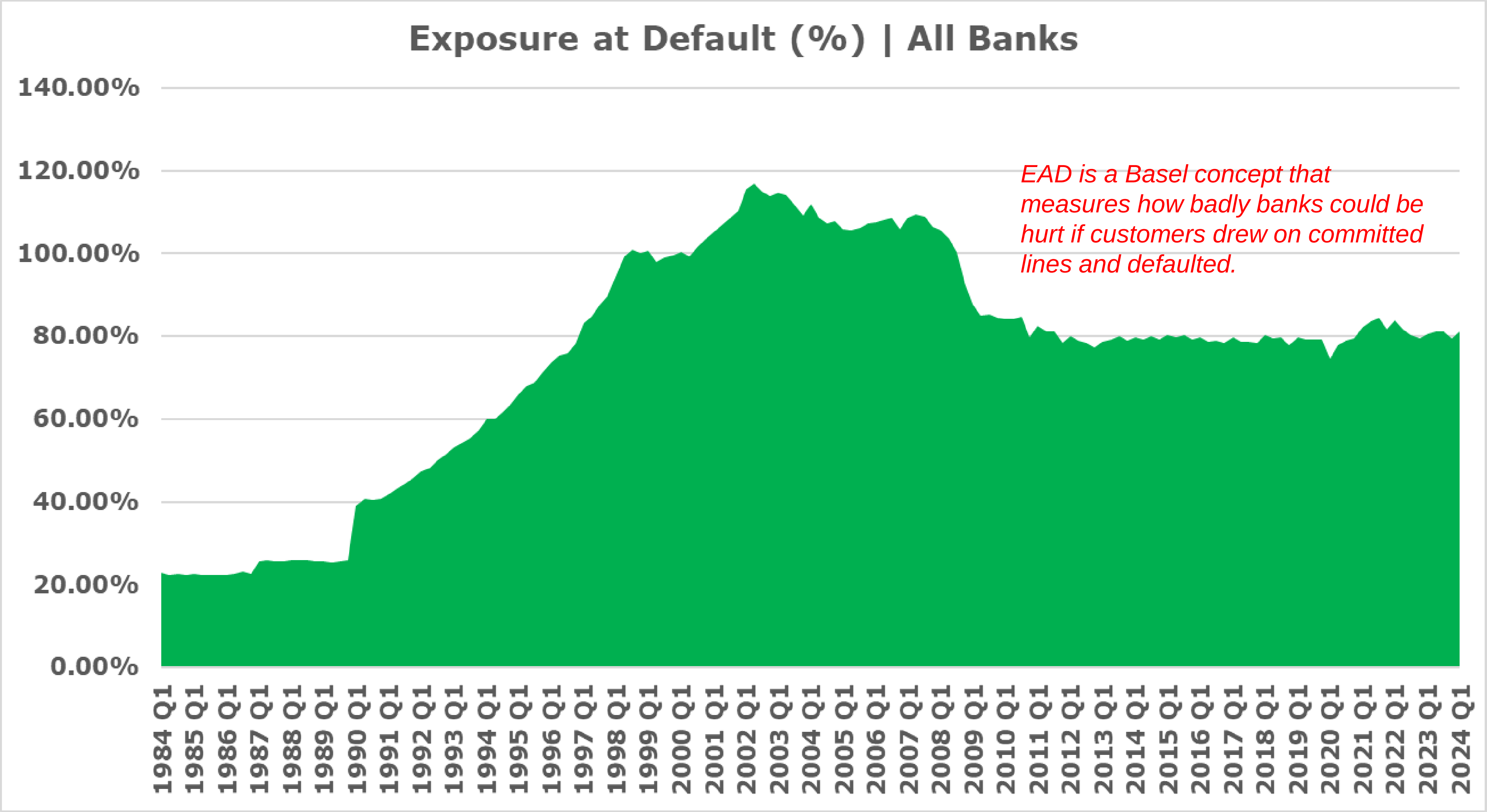
Source: FDIC/ WGA LLC

Exposure at Default (EAD)

- Exposure at default (EAD) illustrates current high risk appetite of banks for consumer and commercial credit. EAD is currently over 80% of total loans & leases in fully committed lines.
- Credit cards and "all other" commercial lines used to purchase new loans and leases are the two largest categories.
- US banks added trillions in unused credit lines since 2020. Despite rising delinquency in consumer exposures, largest banks remain aggressively positioned with almost $10 trillion in undrawn credit.



Source: FDIC

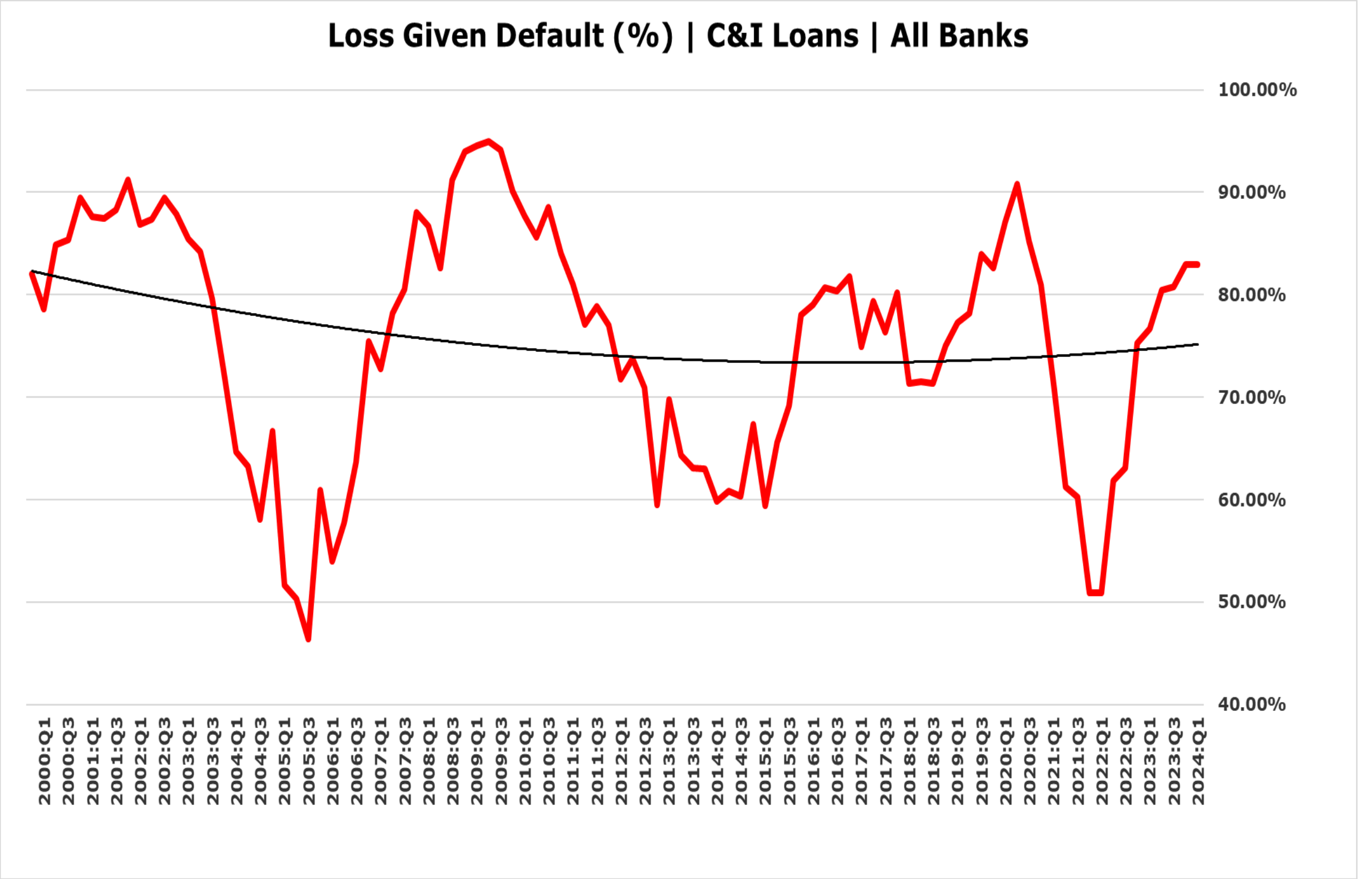


Source: FDIC/WGA LLC

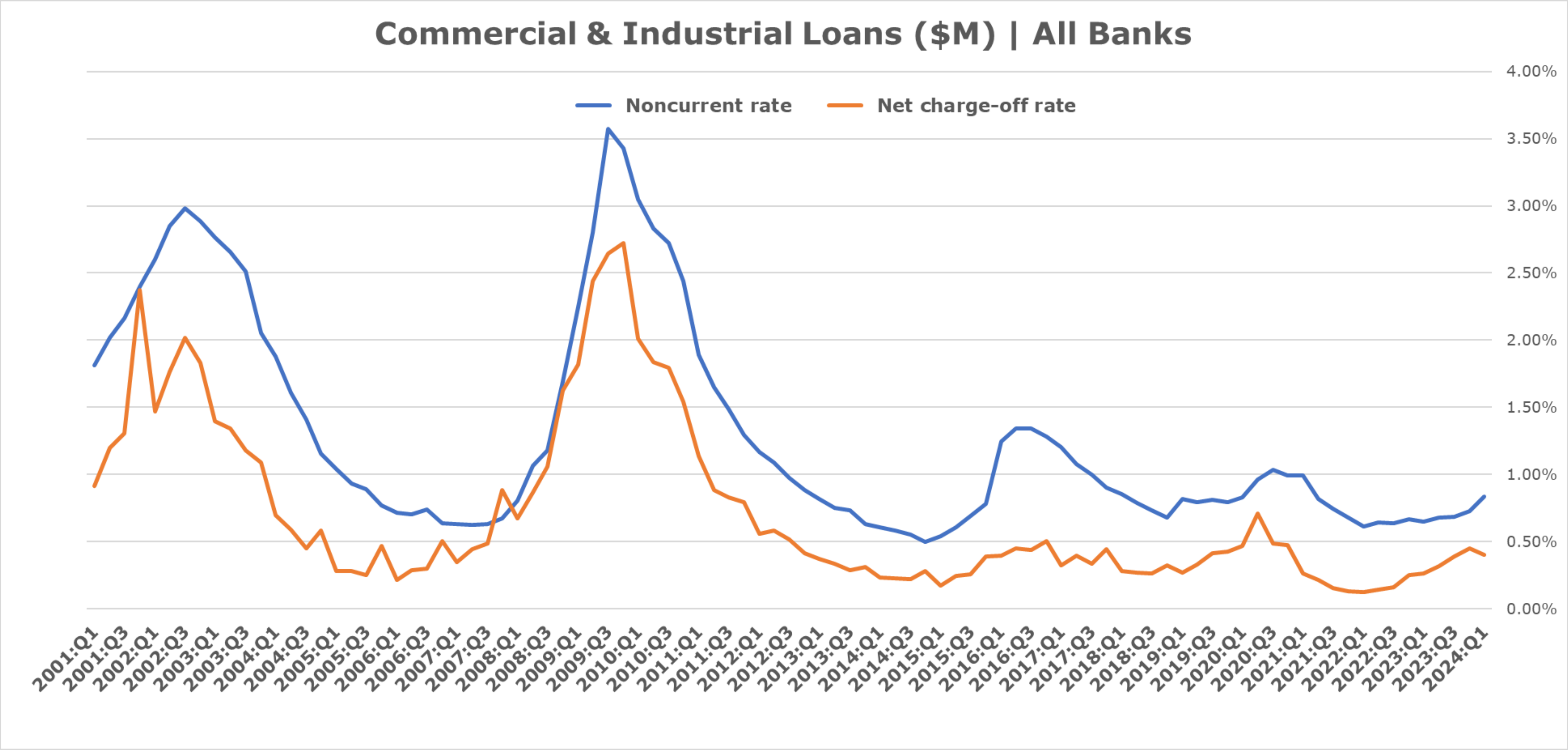
Commercial & Industrial Loans

- The $2.5 trillion C&I category includes secured and unsecured commercial loans other than CRE and is a bellwether for credit in the banking industry and the broader economy. While the net loss rate is rising rapidly, it is still below 2019 and 2008 levels.

- The swings in loss severity for this important data series are significant, with two periods, 2005 and 2021, when loss rates fell to 50% of the unpaid principal balance due to strong collateral prices.



Source: FDIC/WGA LLC


Commercial & Industrial Loans ($M) | All Banks
Noncurrent rate
Net charge-off rate
4.00%
3.50%
3.00%
2.50%
2.00%
1.50%
1.00%
0.50%
0.00%
2001:Q1
2001:Q3
2002:Q1
2002:Q3
2003:Q1
2003:Q3
2004:Q1
2004:Q3
2005:Q1
2005:Q3
2006:Q1
2006:Q3
2007:Q1
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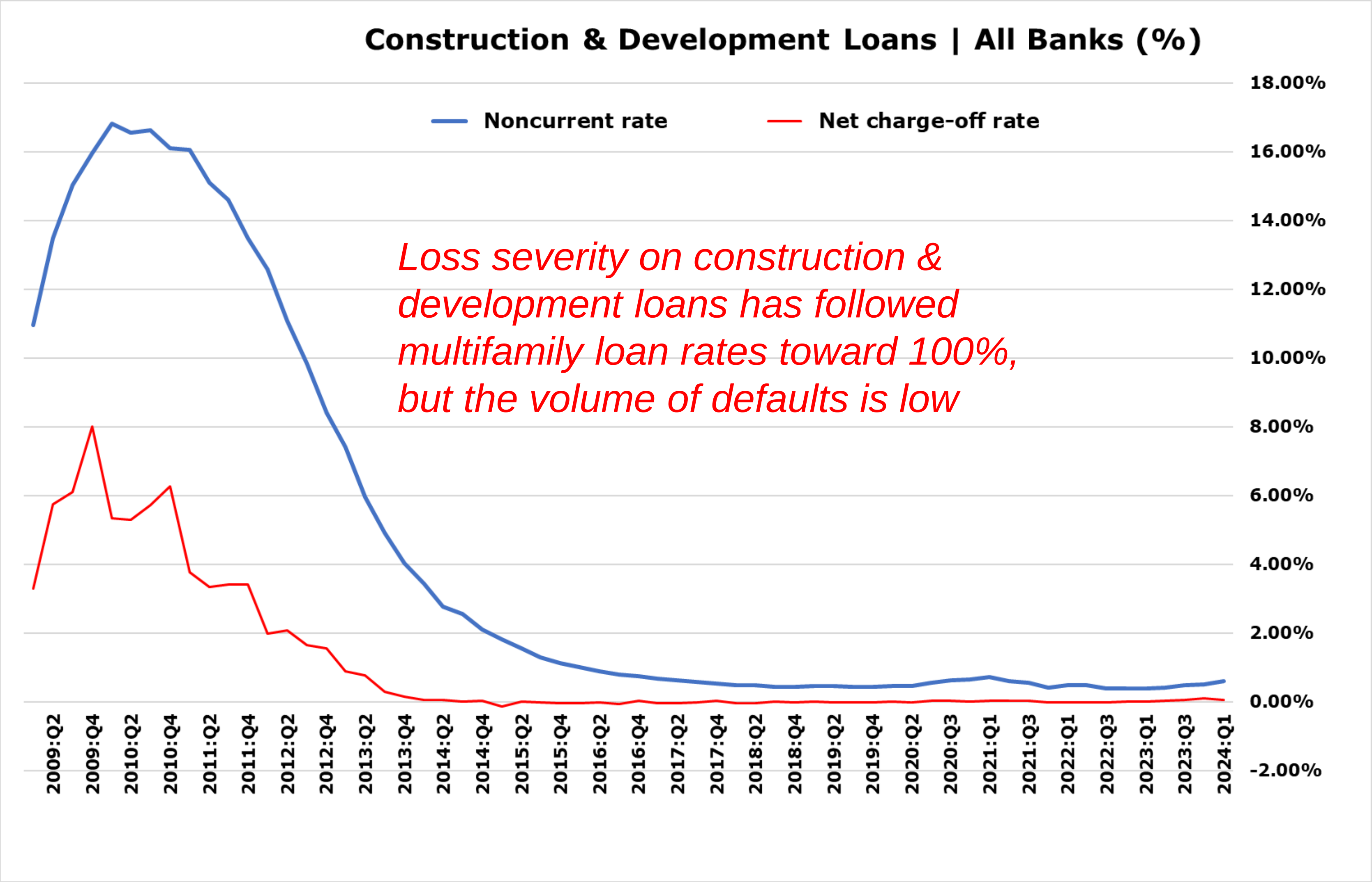
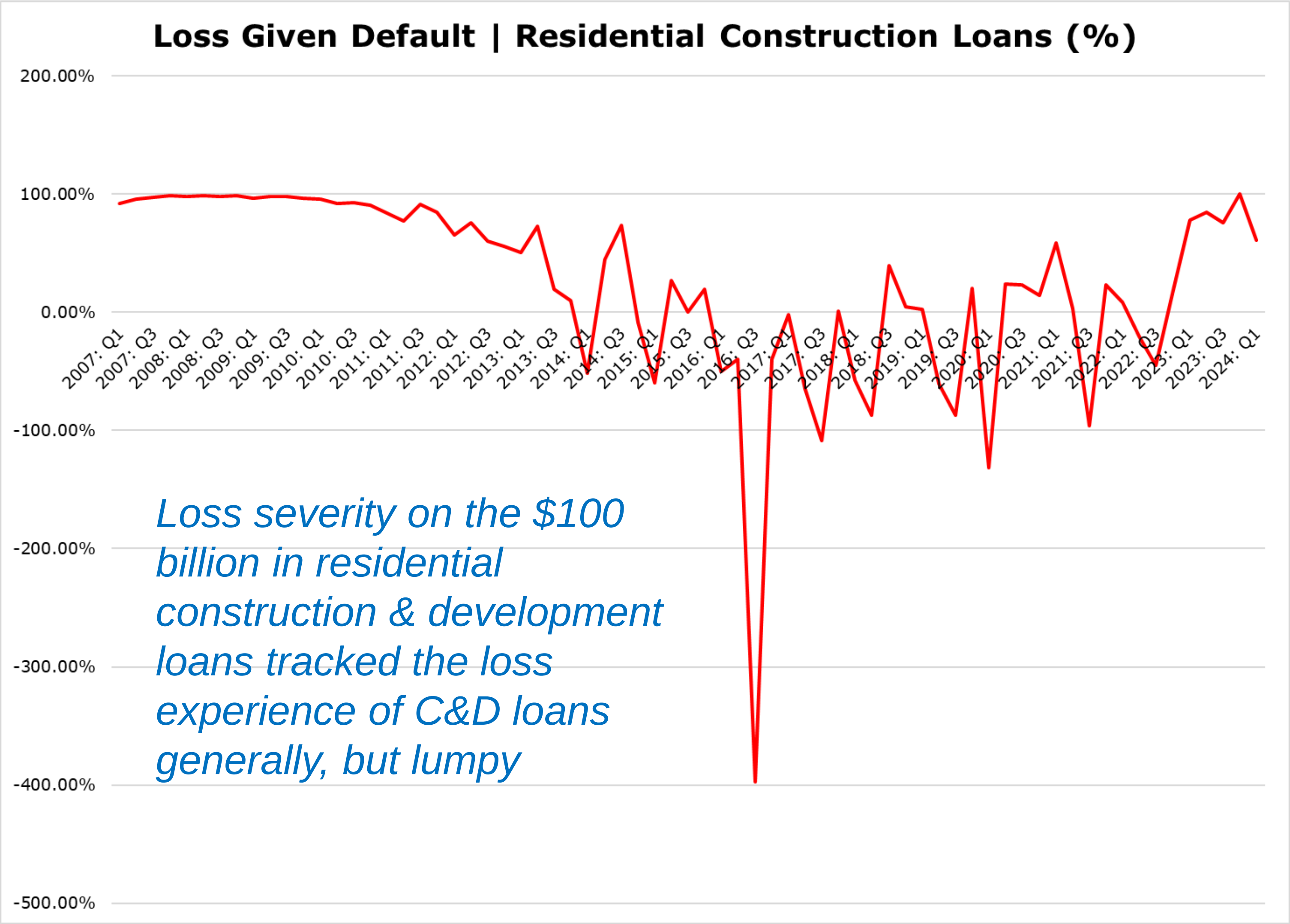
2018:Q3
2019:Q1
2019:Q3
2020:Q1
2020:Q3
2021:Q1
2021:Q3
2022:Q1
2022:Q3
2023:Q1
2023:Q3
2024:Q1

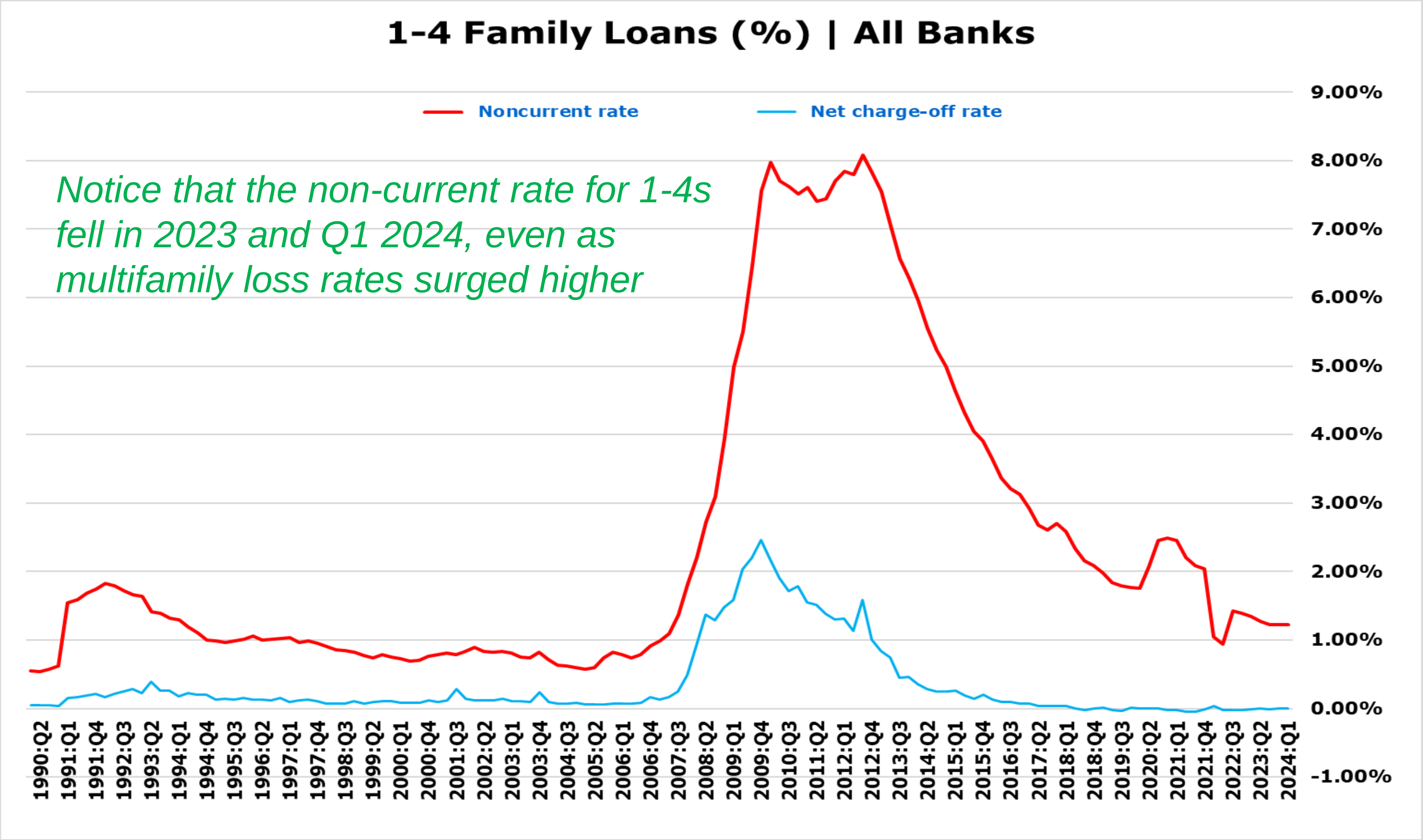
Source: FDIC


Construction & Development Loans | All Banks (%)
Noncurrent rate
Net charge-off rate
Loss severity on construction & development loans has followed multifamily loan rates toward 100%, but the volume of defaults is low
18.00%
16.00%
14.00%
12.00%
10.00%
8.00%
6.00%
4.00%
2.00%
0.00%
-2.00%
2009:Q2
2009:Q4
2010:Q2
2010:Q4
2011:Q2
2011:Q4
2012:Q2
2012:Q4
2013:Q2
2013:Q4
2014:Q2
2014:Q4
2015:Q2
2015:Q4
2016:Q2
2016:Q4
2017:Q2
2017:Q4
2018:Q2
2018:Q4
2019:Q2
2019:Q4
2020:Q2
2020:Q3
2021:Q1
2021:Q3
2022:Q1
2022:Q3
2023:Q1
2023:Q3
2024:Q1

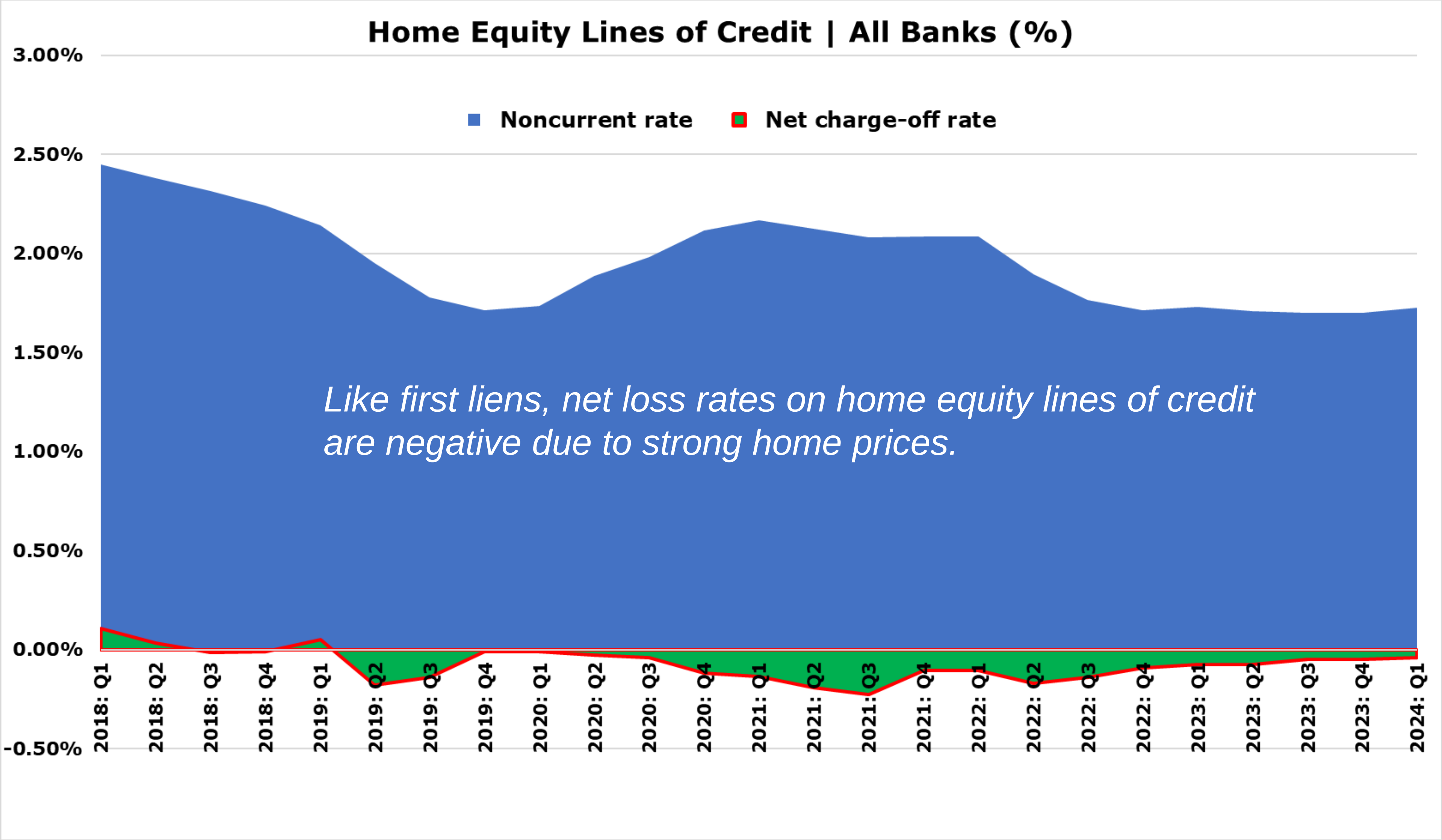
Source: FDIC



Source: FDIC/WGA LLC


1-4 Family Loans (%) | All Banks
Noncurrent rate
Net charge-off rate
Notice that the non-current rate for 1-4s fell in 2023 and Q1 2024, even as multifamily loss rates surged higher
9.00%
8.00%
7.00%
6.00%
5.00%
4.00%
3.00%
2.00%
1.00%
0.00%
-1.00%
1990:Q2
1991:Q1
1991:Q4
1992:Q3
1993:Q2
1994:Q1
1994:Q4
1995:Q3
1996:Q2
1997:Q1
1997:Q4
1998:Q3
1999:Q2
2000:Q1
2000:Q4
2001:Q3
2002:Q2
2003:Q1
2003:Q4
2004:Q3
2005:Q2
2006:Q1
2006:Q4
2007:Q3
2008:Q2
2009:Q1
2009:Q4
2010:Q3
2011:Q2
2012:Q1
2012:Q4
2013:Q3
2014:Q2
2015:Q1
2015:Q4
2016:Q3
2017:Q2
2018:Q1
2018:Q4
2019:Q3
2020:Q2
2021:Q1
2021:Q4
2022:Q3
2023:Q2
2024:Q1

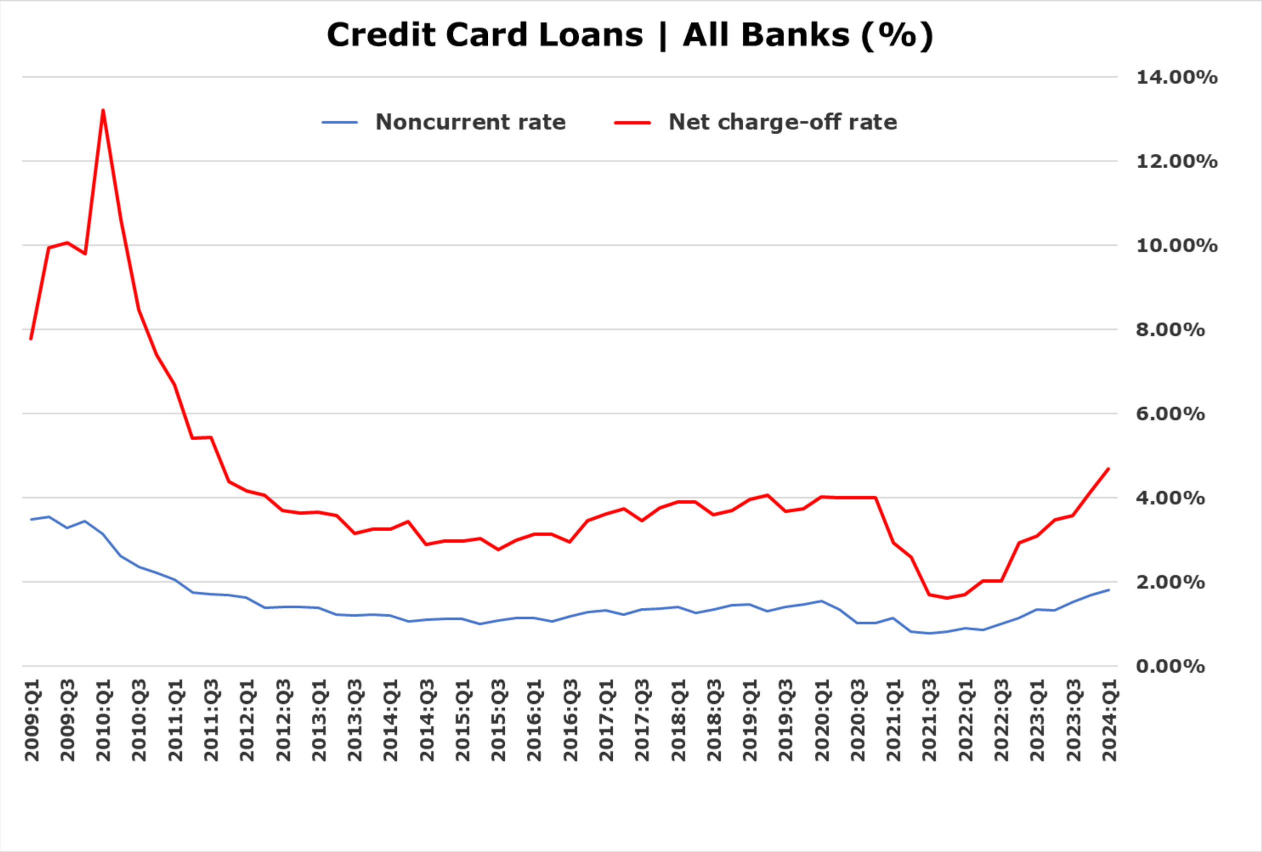
Source: FDIC



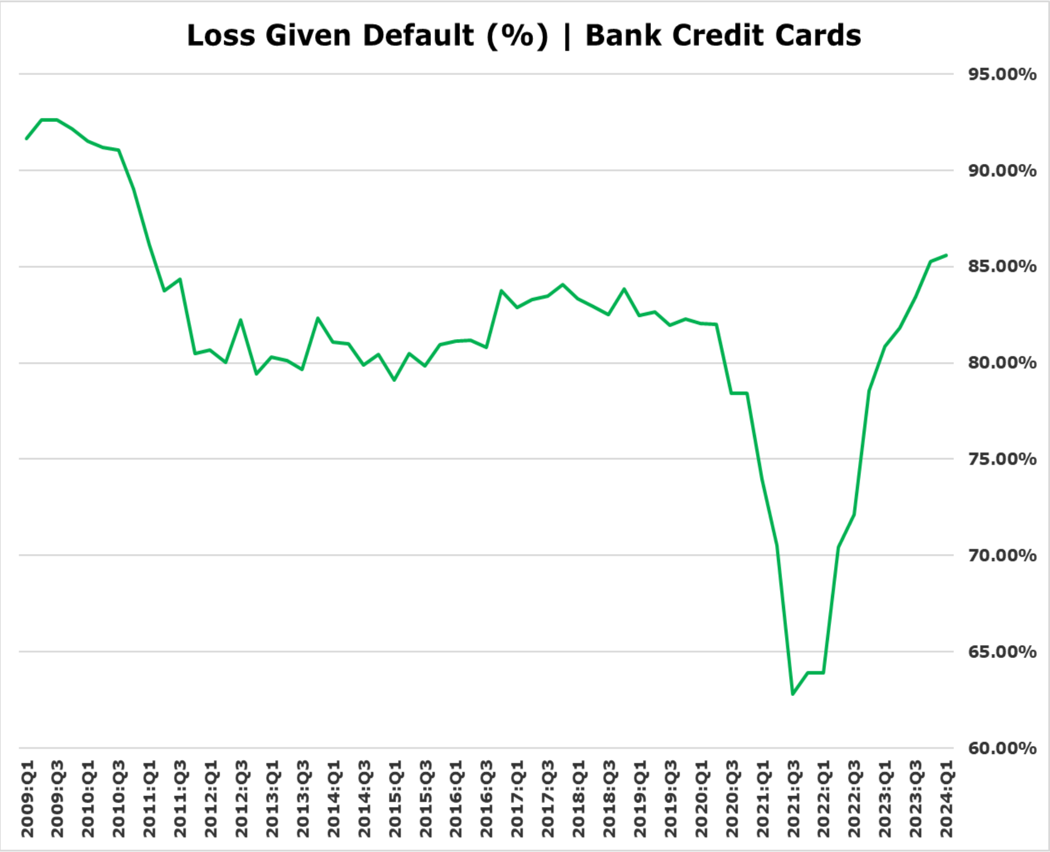
Home Equity Lines of Credit | All Banks (%)
Noncurrent rate
Net charge-off rate
3.00%
2.50%
2.00%
1.50%
1.00%
0.50%
0.00%
-0.50%
2018: Q1
2018: Q2
2018: Q3
2018: Q4
2019: Q1
2019: Q2
2019: Q3
2019: Q4
2020: Q1
2020: Q2
2020: Q3
2020: Q4
2021: Q1
2021: Q2
2021: Q3
2021: Q4
2022: Q1
2022: Q2
2022: Q3
2022: Q4
2023: Q1
2023: Q2
2023: Q3
2023: Q4
2024: Q1
Like first liens, net loss rates on home equity lines of credit are negative due to strong home prices.

Source: FDIC

Loss Rates on Credit Card Receivables Climbing

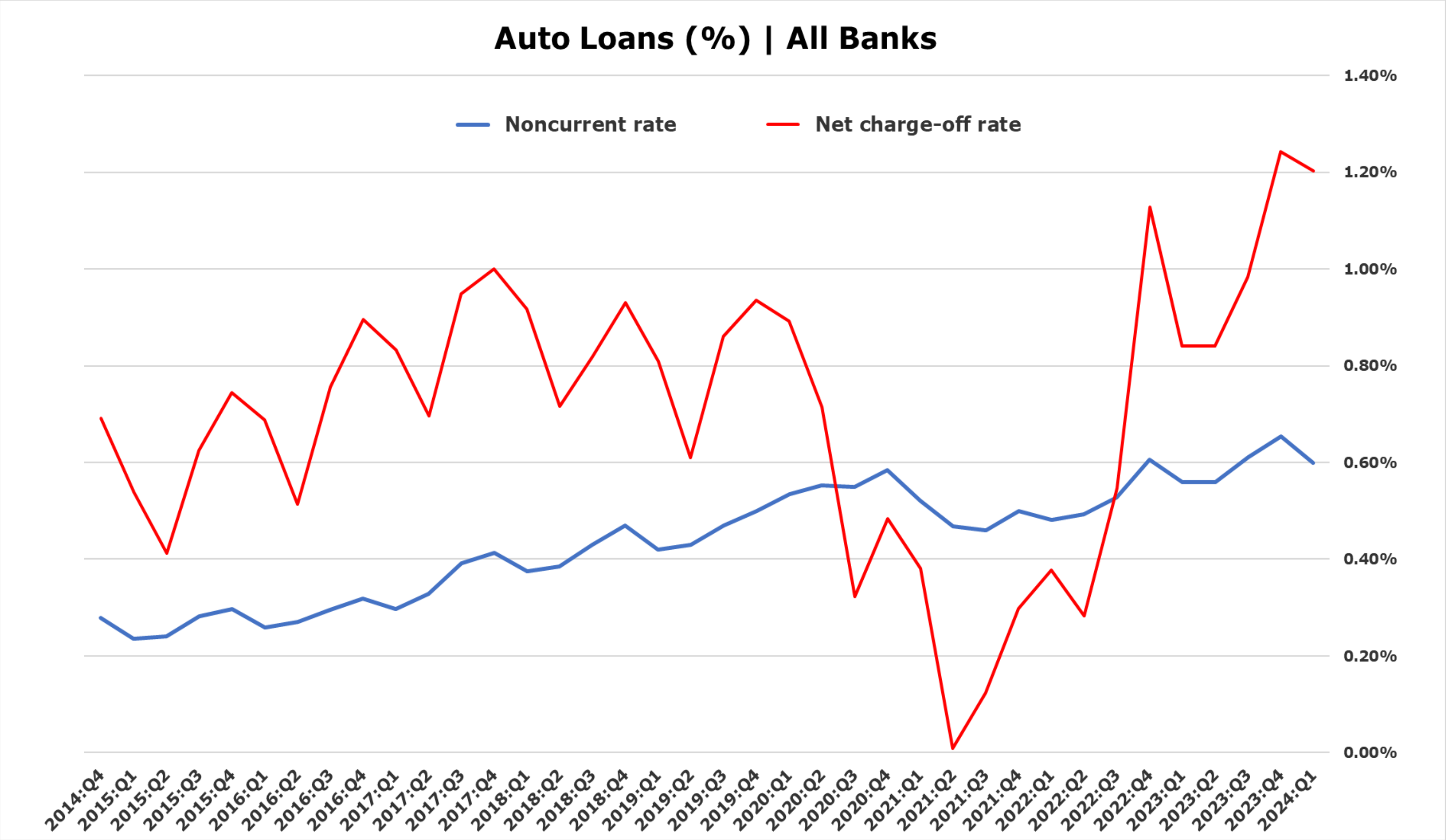


Source: FDIC



Source: FDIC/WGA LLC

Bank Auto Loans



Source: FDIC/WGA LLC

- Bank owned auto loans are a prime, $540 billion asset class and perhaps the single most problematic of the consumer exposures for banks in 2024.

- Loss rates on prime auto loans owned by banks already reached levels *above* pre-COVID, suggesting that this may be the first consumer risk exposure to become a serious negative for bank earnings in 2024 and beyond.

Outlook for 2024

- Over the past several years, the US banking industry has been adjusting to a number of new realities, first and foremost a secular increase in interest rates. The unrealized losses on COVID era securities remain a huge problem for banks large and small as illustrated by the chart on Slide 10. If interest rates rise from current levels, then bank solvency again becomes an issue and may cause increased market volatility.
- The next test for banks is credit, when commercial and consumer exposures are likely to test pre-COVID levels of default. Low interest rates over the past 15 years has masked the reality of limited consumer credit capacity. Next phase of the economy may see credit losses revert to the LT averages and push bank provision expense higher.
- While we do not expect net loss rates to rise to 2008 levels, we do expect to see credit expenses consume a larger and larger portion of bank earnings as provisions grow from current levels. Provisions expenses above $20 billion per quarter may become the norm going into 2025, especially if consumer credit exposures continue to deteriorate in areas such as CRE, credit cards and auto loans.

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Questions? Comments?