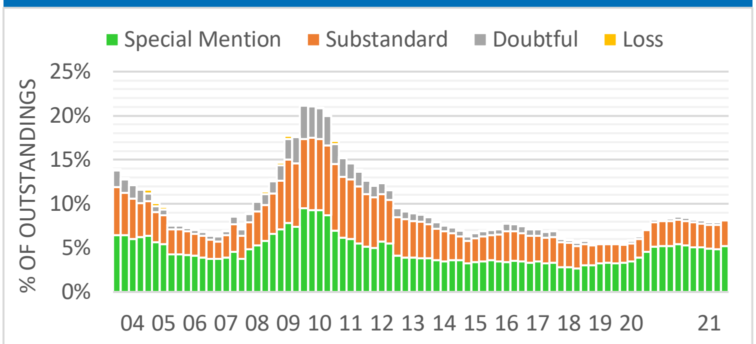
Commercial Credit Quality Bulletin

April 2021

Overall Credit Quality Steady but Pockets of Weakness in Commercial Real Estate Remain

With bank earnings season upon us, revenue, net interest margins, and credit quality are taking center stage. Several of the early bank reporters, after building sizeable credit loss reserves as the economy fell into recession, have started to release reserves as the recovery takes shape. For its part, commercial credit quality continues to hold steady. Short-term delinquencies have continued their general downward trend, and now represent 0.43% of total outstanding loans at the end of 1Q2021, compared to 0.77% in the year-ago period. Nonaccrual loans represented 0.95% of total outstandings at 1Q2021 and have remained relatively stable over the last six months but are still up considerably from 0.71% one year ago.

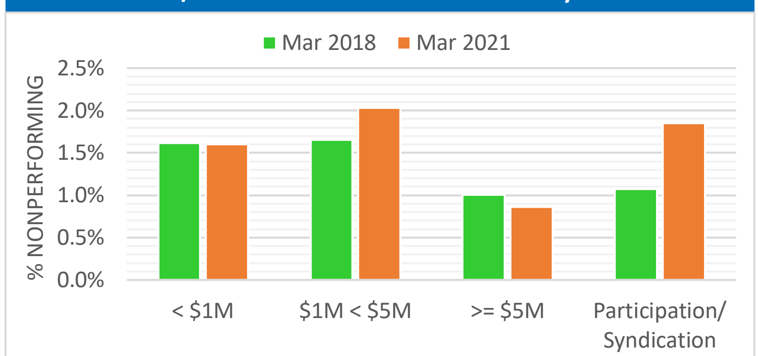
C&I Criticized Loan Trend



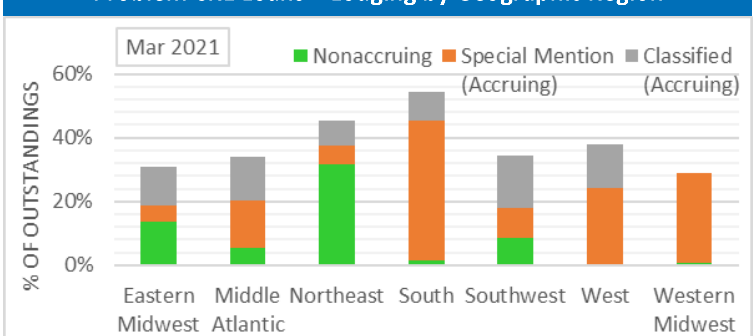
Commercial loans with a criticized risk rating – consisting of those loans rated Special Mention, Substandard, Doubtful, or Loss – increased 6.5% month over month and now represent 8.5% of total outstanding loans. This level is near the current cyclical peak but well off historical high watermarks. While balances in all criticized grades increased month over month, 70% of the increase was in the Special Mention rating, and within that category, the biggest movers were Retail Trade (merchandise retailers) and Real Estate and Rental & Leasing.

The RMA/AFS Performance Index represents the sum of all delinquent and nonaccrual loans as a percentage of total outstandings. During downturns, performance is often correlated with deal size, with larger deals generally performing better than smaller deals. This cycle has been different, with smaller companies benefitting from government assistance programs such as PPP as well as aggressive bank payment deferral programs. As a result, small deal performance is now generally in line with levels seen three years ago during calmer times.

C&I RMA/AFS Performance Index Trend – By Deal Size



Problem CRE Loans – Lodging by Geographic Region



In Commercial Real Estate, it has been the Lodging industry (hotels & motels) that has borne the brunt of the pandemic-induced economic disruption. As a group, the Lodging property type has seen nonaccrual levels reach 9%. Problems are most pronounced in the Southern and Northeastern regions of the country, where the combination of nonaccruing Lodging loans plus those Lodging loans that are still on accrual status but have a criticized loan rating represent over 50% of total outstandings. The national average for this total is closer to 38%.

Why RMA and AFS?

RMA and AFS are committed to providing relevant, timely, and practical credit risk solutions to banks. Combining the strengths of each to offer information and insight, RMA and AFS are ideally situated for collaborations aimed at identifying and responding to the credit risk needs of financial institutions.

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