



Fourth Quarter 2021 Banking Conditions

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Bank earnings remain elevated though have moderated from mid-year highs. The return on average assets (ROAA) for District banks ended the year at 1.36 percent, benefitting from historically low provisions, decreasing interest expense, and cost efficiencies gained in overhead expense as a percent of average assets. District banks pulled back reserve levels throughout the year to the benefit of earnings, after having been built up at the onset of the pandemic. However, declining interest income and noninterest income continue to hinder earnings performance. Net interest margins (NIMs) remain compressed as inflated balance sheets coupled with the low interest rate environment and depressed loan demand has placed downward pressure on asset yields. Yields on both loans and securities continue to decline and outweigh the savings from declines in cost of funds.

Balance sheets continue to grow and remain flush with liquidity though growth has placed pressure on capital ratios. Increasing deposits remains the primary driver of balance sheet growth, while noncore funding continues to decline. Influxes of deposits have been placed in liquid yet low-yielding assets, primarily cash and securities, which now make up 38 percent of assets at District banks. In contrast, loans to assets total only 55 percent, a decrease from 61 percent at the prior year-end. Although outweighed by the continued increase in liquid assets, loan growth turned positive for District banks during the fourth quarter. Continued growth in CLD lending, as well as a pickup in other CRE, agricultural, and consumer lending, contributed to the increase in loans. Further, the decreasing trend in C&I loans is starting to stabilize; C&I growth remained balanced during the fourth quarter, although ended the year 16 percent lower than year-end 2020.

Credit conditions are stable as charge-offs remain low, and past due and nonaccrual loans continue to decrease. Loan loss reserves have declined, representing 1.36 percent of total loans, and are approaching pre-pandemic levels as a result of low or reverse provisioning.
