Highlight: Loan growth is slowing, driven by decreased real estate lending

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Community banks' pace of loan growth, particularly real estate lending, has slowed as loan yields remain elevated.

- Residential and commercial real estate are significant lending segments for community banking organizations (CBOs)[1], comprising 68 percent of CBO loan portfolios at year-end 2024. Various economic factors, including the relationship between higher rates and credit demand, have contributed to a slowdown in overall loan growth for CBOs. Notably, Construction and Land Development (CLD) lending experienced the greatest slowdown with year-over-year growth of 23.44 percent in 2022 declining to only 0.18 percent in 2024.
- Annual growth in other CBO lending segments also slowed in 2024, though to a lesser degree. Annual agricultural and commercial and industrial loan growth declined to 4.81 percent and 4.37 percent in 2024, compared to 6.18 percent and 4.81 percent in 2023, respectively.
- CBOs increased the average interest rate charged on real estate loans from 4.67 percent in 4Q 2022 to 6.03 percent in 4Q 2024 which is generally in line with market rate movements, as evidenced by the 10-year treasury yield increasing from 3.88 percent to 4.58 percent in the same timeframe. Increased interest rates tend to reduce loan demand as financial capacity to service real estate loans tightens. Furthermore, increased market interest rates have pressured bank liquidity positions[2] potentially incentivizing banks to prioritize growth in highly liquid assets ahead of less liquid loans.

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Endnotes

[1] Community banking organizations are defined as having less than $10 billion in total assets.

[2] See Highlight: Losses in securities portfolios remain historically high