DATA DISPATCH

Risk-weighted assets flat as bank balance sheets swell; capital strengthens

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Market Intelligence

U.S. bank capital ratios have continued to march higher as anemic lending helped keep risk-weighted assets about flat in the first half of the year.

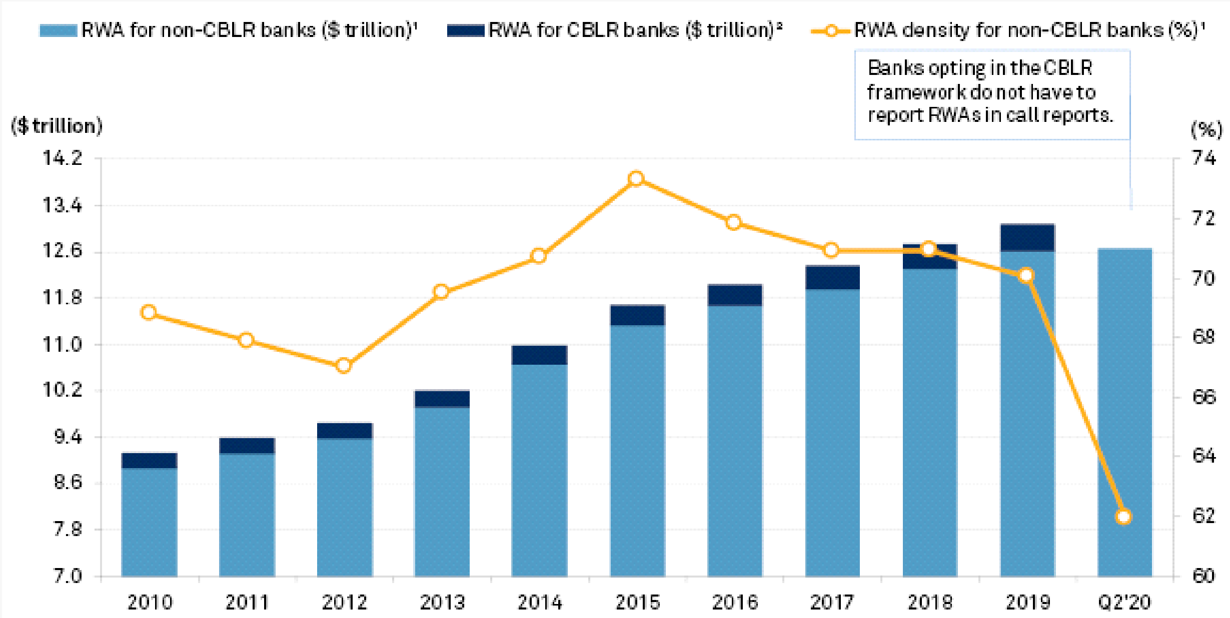
With a pullback on share repurchases because of risks caused by the pandemic, banks have continued to accumulate capital despite earnings that have been weakened by massive credit loss provisions. Across the industry, common equity Tier 1 capital increased $48.51 billion in the first half of 2020, according to data from S&P Global Market Intelligence, nearly as much as in all of 2019 combined. Capital distributions — stock buybacks and dividends — had been approaching 100% of net income before the recession.

Bank balance sheets have ballooned in 2020 as the Federal Reserve bought up bonds to buffer the economy, but the growth has been concentrated in asset categories with low or zero risk weights, including Treasurys and cash. Lending during the pandemic has been weak, except for a surge in corporate borrowing against credit lines with banks that has now completely reversed and about $525 billion in Paycheck Protection Program loans. The PPP loans are fully guaranteed by the government and have a zero-percent risk weight.

Overall, risk-weighted assets increased just 0.3% during the first half of 2020, compared with annual increases that ranged from 2.4% to 7.4% during the preceding nine years. These figures exclude small banks that have elected to use the community bank leverage ratio, or CBLR, which replaces ratios used to measure capital adequacy under the Basel III framework with a single leverage ratio.

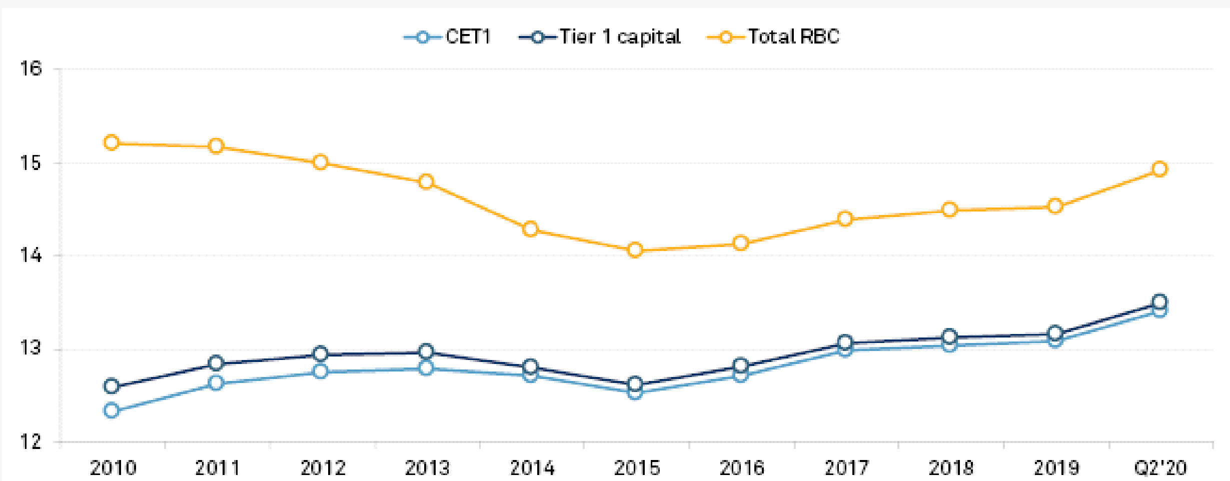
The ratio of risk-weighted assets to total assets for non-CBLR banks plunged 8.1 percentage points in the first half of 2020 to 62%, far below a low of 67% over the preceding decade. In aggregate, non-CBLR banks' CET1 ratio increased 0.3 percentage point to 13.4%, a new high.

Aggregate risk-weighted asset trends for US banks



Data compiled Oct. 13, 2020.
RWA = risk-weighted assets; CBLR = community bank leverage ratio; RWA density = risk-weighted assets as a percentage of total assets
Analysis includes operating and historical U.S. commercial banks, savings banks, and savings and loan associations. Nondepository trusts and companies with a foreign banking organization charter are excluded.
Data based on regulatory filings.
[1] Includes banks that did not opt into the CBLR framework in the second quarter of 2020.
[2] Includes banks that opted into the CBLR framework in the second quarter of 2020.
Changes to the computation of banks' risk-weighted assets under the final Basel III rules took effect Jan. 1, 2015. Prior to the final Basel III rules, U.S. banks reported risk-weighted asset information under general risk-based rules.
Source: S&P Global Market Intelligence

Aggregate risk-based capital ratios for US non-CBLR banks (%)



Data compiled Oct. 13, 2020.
CET1 = common equity Tier 1; CBLR = community bank leverage ratio; RBC = risk-based capital
Analysis includes operating and historical U.S. commercial banks, savings banks, and savings and loan associations that did not opt into the CBLR framework in the second quarter of 2020.
Nondepository trusts and companies with a foreign banking organization charter are excluded.
Data based on regulatory filings.
Changes to the computation of banks' capital ratios under the final Basel III rules took effect Jan. 1, 2015. Prior to the final Basel III rules, U.S. banks reported capital information under general risk-based rules.
Source: S&P Global Market Intelligence

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Investors are eager for banks to resume share repurchases after self-imposed moratoria, followed by a ban for large banks imposed by the Fed. Community banks have started to reinstate buyback programs, and JPMorgan Chase & Co. said it could begin buying back shares again in the first quarter of 2021 if the Fed does not extend its restrictions. Morgan Stanley also said it is positioned to resume shareholder distributions at a more than 100% payout ratio in the first quarter. Truist Financial Corp., however, said it is premature to discuss buybacks and the possibility of dividend increases because of the fragile economic environment.

Capital at almost all the large banks currently exceeds required levels determined by losses projected in the 2020 stress tests. But the Fed is running another round of stress tests to measure resilience to even harsher scenarios meant to simulate possible paths for the pandemic and the economy, including a double dip.

Analysts at Keefe Bruyette & Woods have excluded share repurchases from their estimates for large banks until 2022, but said buybacks are possible for the group in 2021. In a note on Oct. 9, B. Riley FBR analyst Steve Moss said he expects many smaller banks to restart share repurchases in the coming months, citing expectations for lower credit provisions and "limited balance sheet growth."

While bank capital levels have improved in the aggregate and generally remain above regulatory requirements for individual institutions, 11 banks had total capital ratios above the minimum of 8% but below 10.5%, the level prescribed after the inclusion of a 2.5% capital conservation buffer, at June 30. Banks that breach capital conservation buffers are subject to restrictions on the amount of retained income they can distribute to shareholders or use on discretionary bonuses to executives.

In addition, two banks that elected to use the CBLR in the second quarter, and are not subject to Basel III rules anymore, had total capital ratios between 8% and 10.5% at March 31.

Most banks with less than $10 billion in assets are eligible to use the CBLR, but most have not elected to do so. Community banks that have opted to remain subject to the Basel III rules have said switching does not save much time, and rapid deposit growth during the pandemic has strained leverage ratios.

An investor group has agreed to acquire Georgia Banking Co., one of the banks just under the 10.5% threshold with a total capital ratio of 10.45% at June 30.

US banks below the Basel III minimum capital conservation buffer requirement of 2.5%

A banking organization's capital conservation buffer is calculated by taking the lowest of the three: (i) CET1 capital ratio minus minimum CET1 capital ratio requirement, (ii) Tier 1 capital ratio minus minimum Tier 1 capital ratio requirement and (iii) total capital ratio minus minimum total risk-based capital ratio requirement. If any one of these ratios is less than or equal to the applicable minimum requirement, the capital conservation buffer is 0%.

Based on companies that did not opt for CBLR in Q2'20

Company (top-level ticker)	City, state	Q2'20 Total assets ($M)	Q2'20 CET1 capital ratio (%)	Q2'20 Tier 1 capital ratio (%)	Q2'20 Total capital ratio (%)	Capital conservation buffer[1]	Capital conservation buffer[1]: Max payout ratio (%)[2]
	Minimum regulatory thresholds:		4.50	6.00	8.00		
Farmers Bank	Carnegie, OK	85.3	6.93	6.93	8.21	0.21	0.00
Nano Banc	Irvine, CA	1,147.9	8.59	8.59	9.43	1.43	40.00
Citizens Savings Bank and Trust Co.	Nashville, TN	104.1	8.29	8.29	9.55	1.55	40.00
Peoples Bank & Trust Co. of Hazard	Hazard, KY	254.1	8.80	8.80	10.05	2.05	60.00
Farmers & Merchants Bank	Lakeland, GA	611.3	8.83	8.83	10.09	2.09	60.00
Bank of Louisiana (BOLB)	New Orleans, LA	85.5	8.88	8.88	10.14	2.14	60.00
First National Bank and Trust Co. of Vinita	Vinita, OK	347.3	8.90	8.90	10.17	2.17	60.00
American Bank of Oklahoma	Collinsville, OK	364.2	9.07	9.07	10.32	2.32	60.00
Citizens State Bank	Hudson, WI	262.1	9.19	9.19	10.38	2.38	60.00
BayCoast Bank	Swansea, MA	2,126.2	9.65	9.65	10.44	2.44	60.00
Georgia Banking Co.	Sandy Springs, GA	704.6	10.06	10.06	10.45	2.45	60.00
Industry median[3]			**14.46**	**14.47**	**15.59**	**7.58**	

Based on companies that opted for CBLR in Q2'20

Company (top-level ticker)	City, state	Q2'20 total assets ($M)	Q1'20 CET1 capital ratio (%)	Q1'20 Tier 1 capital ratio (%)	Q1'20 Total capital ratio (%)	Capital conservation buffer[1]	Capital conservation buffer[1]: Max payout ratio (%)[2]
	Minimum regulatory thresholds:		4.50	6.00	8.00		
Main Street Bank (KEFI)	Bingham Farms, MI	333.4	9.51	9.51	9.51	1.51	40.00
United Texas Bank	Dallas, TX	958.7	9.90	9.90	10.47	2.47	60.00
Industry median[4]			**16.58**	**16.58**	**17.83**	**9.83**	

Data compiled Oct. 13, 2020.
CET1 = common equity Tier 1; CBLR = community bank leverage ratio
Analysis based on all operating U.S. commercial banks, savings banks, and savings and loan associations. Nondepository trusts and companies with a foreign banking organization charter are excluded. Institutions with a zero percent capital conservation buffer are not shown.
Data based on regulatory filings.
Values in orange denote the lowest of the three ratios relative to the minimum requirements used in the capital conservation buffer calculation.
[1] Under the final Basel III rules, banks and thrifts must hold a capital conservation buffer above minimum risk-based capital requirements to avoid limitations on distributions, including dividend payments and certain discretionary bonus payments to executive officers.
[2] Percentage of eligible retained income that a banking institution can pay out in the form of distributions and discretionary bonus payments during the current calendar quarter. The maximum payout ratio is based on the banking institution's capital conservation buffer.
[3] Includes all operating U.S. commercial banks, savings banks, and savings and loan associations that did not opt into the CBLR framework in the second quarter of 2020. Excludes nondepository trusts and companies with a foreign banking organization charter.
[4] Includes all operating U.S. commercial banks, savings banks, and savings and loan associations that opted into the CBLR framework in the second quarter of 2020. Excludes nondepository trusts and companies with a foreign banking organization charter.
Source: S&P Global Market Intelligence

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