

# CECL Reserving and Credit Benchmarking Quarterly Study

FOURTH-QUARTER 2020



COVID-19's adverse impact on loan performance and current Coronavirus Aid, Relief, and Economic Security (CARES) Act financial reporting and disclosure relief arrived simultaneous to the implementation of the controversial Current Expected Credit Losses (CECL) accounting standard for loan-loss reserving. Analysis and comparisons would have been difficult under any of these circumstances. However, the interplay of all three factors has made analyzing bank loan performance and reserving levels even more difficult.

In a continuing effort to provide financial statement preparers and users more insightful information to benchmark activity better across a representative cross-section of banks (given asset size, geographic location, and business mix), Berkeley Research Group's (BRG) Financial Institution Advisory practice created the quarterly *CECL Reserving and Credit Benchmarking Study*. The study compares allowance levels, charge-offs, nonperforming loans (based on CARES Act classification/reporting relief), COVID deferrals, and other key credit metrics across multiple predominately domestic US institutions.

This third study in our series continues to analyze the same twelve representative banks that appeared in our first two studies. These banks have total assets as of December 31, 2020, ranging from \$30 billion to \$467 billion (and a \$102 billion median).

## Key observations from this fourth-quarter study include:

- ✓ Coverage ratios fell slightly during Q4 2020 when compared to Q3 2020, but still are approximately 50 basis points (bp) higher than pre-pandemic levels, on average.
- ✓ Allowance coverage ratios continue to vary widely, with a difference of more than four times the lowest and highest bank in our survey.
- ✓ Commercial loans still are up almost 10% from prior-year levels due to COVID Paycheck Protection Program (PPP) lending, but they did decrease 152 bp on average during Q4 2020.
- ✓ COVID deferral amounts continued to decrease significantly this period, falling (in total) 59% and 90% on average from that observed in the third and second quarters, respectively.
- ✓ Commercial real estate COVID deferrals continue to be the most pronounced areas of stress, with ranges of 68 bp to 2.62% of the portfolio deferred.
- ✓ COVID deferrals as a percentage of loans now range from 26 bp to 1.38%.
- ✓ Consumer COVID deferrals are starting to challenge commercial real estate as the most pronounced area, with ranges from 44 bp to 2.25% of the portfolio deferred.
- ✓ Three of twelve banks in our survey released provisions during Q4 2020, and one recorded a provision of zero.
- ✓ Nonperforming loans increased only slightly during the quarter: 3 bp on average. However, the low balance stayed essentially flat, while the high balance increased 86 bp from Q3 to Q4 2020.
- ✓ Charge-off ratios are still benign, with a 7 bp quarterly reduction on the average ratio noted. However, there was more disparity in reported charge-offs across institutions this quarter.

## Detailed Data Comparisons

### Coverage Ratios as of December 31, 2020<sup>1</sup>

	Low	Median	Average	High
Loan Allowance to Loan Portfolio	0.56%	1.56%	1.68%	2.25%
Total Allowance <i>(including for off-balance commitments)</i> to Loan Portfolio	0.59%	1.76%	1.82%	2.46%
Commercial Allowance Coverage Ratio	1.01%	1.67%	1.88%	2.98%
Consumer Allowance Coverage Ratio	0.23%	1.45%	1.62%	2.76%

### Increase in Total Allowance Coverage Ratios<sup>2</sup>

	Low	Median	Average	High
Loan Allowance – 4Q to 3Q	–0.02%	–0.06%	–0.02%	–0.07%
Loan Allowance – 4Q to 2Q	–0.02%	–0.06%	0.02%	0.05%
Loan Allowance – 4Q to 1Q	0.00%	0.07%	0.20%	0.26%
Loan Allowance – 4Q to 4Q 2019 <i>(post-CECL)</i>	0.02%	0.45%	0.48%	0.51%
Total Allowance – 4Q to 3Q	–0.01%	–0.03%	–0.02%	–0.12%
Total Allowance – 4Q to 2Q	–0.01%	0.02%	0.03%	0.09%
Total Allowance – 4Q to 1Q	0.00%	0.15%	0.23%	0.32%
Total Allowance – 4Q to 4Q 2019 <i>(post-CECL)</i>	0.03%	0.55%	0.54%	0.56%

### Change in Commercial Loan Portfolio

*(impact of PPP loans)*

	Low	Median	Average	High
Increase in Total Commercial Loans – 4Q to 3Q	–4.71%	–2.37%	–1.52%	6.66%
Increase in Total Commercial Loans – 4Q to 2Q	–8.30%	–3.01%	–3.11%	7.95%
Increase in Total Commercial Loans – 4Q to 1Q*	–11.31%	3.27%	1.76%	15.22%
Increase in Total Commercial Loans – 4Q to 4Q 2019*	–1.12%	5.80%	9.91%	21.27%

\* Excludes South State for 1Q 2020 and 4Q 2019 due to the acquisition of CenterState Bank as of June 7, 2020.

### Disclosure of COVID Deferrals

- ✓ Eleven of twelve banks disclosed total COVID deferrals.
- ✓ One bank disclosed only total outstanding PPP loans and not total COVID deferrals.
- ✓ Eight of the eleven banks broke out COVID deferrals by primary portfolio areas (therefore, three banks only presented amounts in total).

<sup>1</sup> The fourth-quarter median for sixty-one banks with assets over \$1 billion regulated by the Office of the Comptroller of the Currency (OCC) was 1.37% at December 31, 2020, down 1 bp from that observed at June 30, 2020. Information obtained from Jeffrey Geer, Associate Chief Accountant, OCC.

<sup>2</sup> Represents the actual change in the low-, median-, average-, and high-coverage ratio from one period to the other (therefore, 2.00% in Q4 to 1.50% in Q4 = 0.50% decrease). Some individual banks may have larger or smaller movements than that noted above.

## COVID Deferral Statistics

(as of December 31, 2020)

	Low	Median	Average	High
Commercial and Industrial Loans	0.01%	0.28%	0.53%	2.16%
Commercial Real Estate Loans	0.68%	0.78%	1.18%	2.62%
Equipment Lease Financing	0.16%	0.16%	0.16%	0.16%
Consumer Loans*	0.44%	1.35%	1.30%	2.25%
<b>Total COVID Deferrals</b>	<b>0.26%</b>	<b>0.94%</b>	<b>0.77%</b>	<b>1.38%</b>

\* Excludes Sterling, which has a relatively small consumer portfolio but high COVID deferrals of 6.83%.

## Change in COVID Deferrals

(detail from December 31, 2020)<sup>3</sup>

	Low	Median	Average	High
Commercial and Industrial Loans	-93%	-57%	-46%	-14%
Commercial Real Estate Loans	-58%	-74%	-70%	-63%
Equipment Lease Financing	13%	13%	-91%	-97%
Consumer Loans	-60%	-51%	-50%	-42%
<b>Total COVID Deferrals – 4Q to 3Q</b>	<b>-50%</b>	<b>-47%</b>	<b>-59%</b>	<b>-63%</b>
<b>Total COVID Deferrals – 4Q to 2Q</b>	<b>-94%</b>	<b>-84%</b>	<b>-90%</b>	<b>-91%</b>

\* Excludes Sterling, which has a relatively small consumer portfolio but high COVID deferrals of 6.83%.

## Nonperforming Loan Statistics

(clearly impacted by CARES Act reporting relief)<sup>4</sup>

	Low	Median	Average	High
Commercial and Industrial Loans	0.03%	0.68%	0.75%	2.27%
Commercial Real Estate Loans	0.06%	0.46%	0.58%	1.59%
Equipment Lease Financing	0.10%	0.38%	1.04%	3.22%
Consumer Loans	0.06%	0.72%	0.83%	1.82%
OREO and Foreclosed Assets	0.00%	0.02%	0.04%	0.13%
<b>Total Nonperforming Loans (as of December 31, 2020)</b>	<b>0.16%</b>	<b>0.73%</b>	<b>0.75%</b>	<b>2.06%</b>
<b>Allowance for Loan and Leases to Total Nonperforming Loans (as of December 31, 2020)</b>	<b>78%</b>	<b>273%</b>	<b>306%</b>	<b>647%</b>
Change in nonperformers – 4Q to 3Q	0.01%	-0.06%	0.03%	0.86%
Change in nonperformers – 4Q to 2Q	0.00%	0.03%	0.07%	0.89%
Change in nonperformers – 4Q to 1Q	0.03%	0.11%	0.14%	0.84%
Change in nonperformers – 4Q to 4Q 2019	0.01%	0.10%	0.19%	1.17%

<sup>3</sup> Represents the percentage change in the ratio of COVID deferrals from one period to the other (therefore, 2.00% in Q2 to 0.50% in Q3 = 75% reduction) for low, median, average, and high categories. Some individual banks may have larger or smaller movements than that noted above.

<sup>4</sup> Change in nonperformers represents the actual change in the coverage ratio from one period to the other (therefore 1.50% in Q2 to 2.00% in Q3 = 0.50% increase) for the low, median, average, and high categories. Some individual banks may have larger or smaller movements than that noted above.

## Net Quarterly Charge-Off Metrics<sup>5</sup>

	Low	Median	Average	High
Commercial Charge-Offs to Avg Loans* (annualized)	0.01%	0.25%	0.49%	2.04%
Consumer Charge-Offs to Avg Loans* (annualized)	0.01%	0.23%	0.32%	1.04%
<b>Total Net Charge-Offs to Avg Loans (annualized)</b>	<b>0.01%</b>	<b>0.40%</b>	<b>0.33%</b>	<b>0.61%</b>
Number of Quarters of Charge-Off in Allowance**	4	22	27	56
Change in Charge-off % - 4Q to 3Q	0.00%	0.09%	-0.07%	-0.66%
Change in Charge-off % - 4Q to 2Q	0.01%	0.07%	0.00%	-0.33%
Change in Charge-off % - 4Q to 1Q	0.00%	0.16%	0.03%	-0.43%
Change in Charge-off % - 4Q to 4Q 2019	0.01%	0.14%	0.07%	-0.15%

\* Excludes Frost because 4Q 2020 net charge-offs are not disaggregated between commercial and consumer.

\*\* Excludes First Republic, South State, and Frost, which have outlier balances (given low denominator).

## Change in Provision for Credit Losses<sup>6</sup>

	Low	Median	Average	High
Percentage Increase in Provision - 4Q to 3Q	-588%	-68%	-110%	23%
Percentage Increase in Provision - 4Q to 2Q	-140%	-86%	-82%	13%
Percentage Increase in Provision - 4Q to 1Q	-128%	-92%	-87%	-27%
Percentage Increase in Provision - 4Q to 4Q 2019 #	-770%	-28%	-59%	411%

# Pre-CECL (therefore under the incurred loss model).

## Methodology

All amounts were obtained from publicly available information contained on the banks' websites, including:

- ✓ Security and Exchange Commission Forms 10-Q and 10-K
- ✓ Press releases
- ✓ Earnings presentations
- ✓ Supplemental quarterly financial data

## Benchmarked Banks

✓ PNC	✓ South State	✓ TCF
✓ Citizens	✓ Prosperity	✓ Huntington
✓ Fifth-Third	✓ First Republic	✓ Key
✓ Sterling	✓ Zions	✓ Frost

***Underlying data with respective sourcing is available from BRG upon request and includes breakouts by portfolio category where presented.***

5 Change in charge-off percentage represents the actual change in the charge-off ratio from one period to the other (therefore, 0.94% in Q2 to 1.27% in Q3 = 0.33% increase) for the low, median, average, and high categories. Some individual banks may have larger or smaller movements than that noted above.

6 Represents the percentage change in the provision for loan loss from one period to the other (therefore, \$100 million in Q2 to \$20 million in Q3 = 80% reduction) for low, median, average, and high categories. Some individual banks may have larger or smaller movements than that noted above.



## About BRG

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