A Year in Review

FOR BANKERS, 2018 was a turning point. Bankers noted a number of factors—weaker growth in loan demand, higher funding costs, more competition for deposits—that underscored a much tougher environment for the industry.

A Sustained Decline
Bank leaders’ optimism about their institutions’ experiences over the prior 12 months has been in a slow but steady decline since Q1 2015. This decline accelerated significantly over the course of 2018, reflecting a more challenging environment for banks. While the Bank Experience IndexSM fell below neutral earlier in the year, to 47.4 at the end of Q1, by Q4 it had dropped nearly five points to 42.5, its lowest level since the survey was launched in 2015.

Funding Costs and Deposit Competition Rose
In the fourth quarter of 2018, 91% of bank leaders surveyed reported an increase in their bank’s funding costs—a 13-percentage-point increase year over year. Not surprisingly, most banks reported that deposit competition had also tightened. By year-end, 86% of respondents said that deposit competition had increased during the year, up 23 percentage points from the fourth quarter of 2017 (63%).

Access to Capital Largely Unchanged
Throughout 2018, roughly 70% of bank leaders consistently said their bank’s access to capital was the same compared to 12 months prior. That said, there was a marked decline in the number of bank executives reporting improvement (20% at the end of 2018 vs. 35% at the end of 2017), as well as a large rise in the number of bankers reporting that conditions had worsened (5% vs. 1% for that same time period).

Outlook on Overall Economic Conditions Grew More Pessimistic in 2018
While 76% of bank leaders surveyed said that overall economic conditions for their banks were either the same or improved compared to 12 months prior, nearly one-quarter (24%) reported that conditions were either moderately or significantly worse, representing an 18-percentage-point increase vs. the same time in 2017.

Increase in Loan Demand Slowed
While around one-quarter of respondents reported that loan demand remained largely the same over the course of the year, the number of those who reported an increase compared to 12 months ago was down. In fact, only 43% of respondents reported an increase in loan demand in the fourth quarter of 2018, compared to 58% at the same time last year.

1 Promontory Interfinancial Network’s proprietary Bank Experience Index is calculated by measuring banker experiences for the prior 12 months in four key areas: access to capital, loan demand, funding costs, and deposit competition.
DESPITE SOME POSITIVES IN 2018, banker optimism about the future declined throughout the year.

Each quarter, the Bank Executive Business Outlook Survey asks bank CEOs, CFOs, and presidents what their outlook is for the upcoming 12 months relating to four key factors: access to capital, loan demand, funding costs, and deposit competition. This projection of future conditions is based on respondents’ expectations from data collected between Q4 2017 to Q4 2018.

Bank Confidence in Steady Decline
The Bank Confidence IndexSM is based on expectations for access to capital, loan demand, funding costs, and deposit competition 12 months ahead. The Index reached its lowest point since the inception of the Bank Executive Business Outlook Survey (43.0) by the end of 2018. Confidence declined in each quarter of the year and was not limited to any one region of the country. Expectations for all regions ended the year down, led by the Northeast at 42.5. (Charted on a scale of 0-100, a score of 50 represents the baseline expectation.)

Optimism for Loan Demand Waned
While expectations for loan demand began at a near all-time high with 64% of respondents from the Q4 2017 survey foreseeing an increase, the rest of 2018 told a very different story. Optimism steadily decreased over the course of the year, dropping 25 percentage points to 39% in the fourth quarter of 2018.

Funding Costs Expected to Rise
Eighty-eight percent of bankers—nearly 9 in 10—projected higher funding costs over the coming year. Though high in general, this figure is in line with 2017 levels and lower than the 92-95% benchmarks recorded for the first three quarters of 2018.

Deposit Competition Also Expected to Increase
Not surprisingly, bankers forecasted stronger deposit competition for 2019. However, while still quite high at the end of 2018 (83%), the percentage of bankers expecting a more competitive environment in 2019 was down from the levels recorded earlier in the year (88-90%).

Access to Capital Expected to Remain the Same, But...
While most bank leaders said they expect access to capital to remain the same over the coming year, more felt that way at the end of 2018 (75%) than 2017 (62%). The number expecting more difficult access grew notably from 1% at the end of 2017 to 9% at the end of 2018. At the same time, the number of those who expect to see access to capital improve dropped from 37% in Q4 2017 to 17% in Q4 2018.

Pessimism for Overall Economic Conditions
Banker optimism about overall economic conditions steadily declined throughout 2018, even though 52% of bank leaders do not expect the next recession to begin until sometime in 2020. In Q4 2018, just 22% of bankers expected overall economic conditions to improve over the next 12 months. This is the lowest level recorded since Promontory Interfinancial Network began tracking this indicator and represents a 43-percentage-point decrease from a year earlier. At the same time, the number of respondents expecting conditions to worsen grew approximately seven-fold from 5% to 37%. 

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CAUTIONOUS OUTLOOK FOR THE INDUSTRY

Every region ended lower than where it started in 2018. Bankers in the Northeast led the nation in pessimism, ending at 42.5 in the fourth quarter, closely followed by the West (42.7) and Midwest (42.8). Bankers in the South were less pessimistic than their counterparts, though they experienced the biggest decline in confidence from the Q4 2017 (almost 10 points, -20%).
RELATIVELY STEADY WITH A DROP AT THE END

After a drop in the first quarter, expectations regarding access to capital remained steady throughout 2018. But in the fourth quarter, the number of respondents who expect access to capital to improve over the next 12 months dropped by seven percentage points from the prior quarter (driven by banks in the South and West) and by 20 percentage points from the start of the year.
HOPES FOR THE FUTURE REMAIN, BUT ARE MORE MUTED NOW

What a change from a year ago. Last year a whopping 64% of respondents predicted an improvement in loan demand for 2018. This year only 39% expected to see an improvement in the indicator over the next 12 months. Perhaps more worrisome is the fact that 27% of banks forecasted moderate or significant decreases in loan demand for 2019; that figure is 21 percentage points higher than at the start of 2018.
EXPECTATION FOR HIGHER COSTS REMAINS

At the end of 2018, 88% of respondents expected funding costs to rise, down slightly from recent quarters, but in line with predictions from the beginning of the year.
Expectations for deposit competition remained relatively stable—at high levels—for the past year. Banks in the South predicted the biggest change (worsening) over the course of 2018. The majority of bank leaders expect deposit competition to increase in 2019, led by those in the Midwest and the Northeast.
When asked to rate their expectations for the economy, bankers were pessimistic. After reaching a high of 65% in Q4 2017, the number of bankers expecting economic conditions to improve dropped to a new low of 22% by Q4 2018. All regions recorded declines in expectations for improvement. The most notable change in outlook occurred in the Northeast, where the percentage of bankers forecasting improvement fell from 74% at the end of 2017 to just 5%—a small fraction of what other regions projected—at the end of 2018.
THE SURVEY

The Bank Executive Business Outlook Survey is completed on a quarterly basis and incorporates responses from hundreds of unique banks as provided by bank CEOs, presidents, and CFOs from across the country. The survey is published by Promontory Interfinancial Network. Data is released every quarter. Access the Promontory Interfinancial Network Bank Executive Business Outlook Survey reports online at www.promnetwork.com/research-insights/bank-survey-reports.

All percentages have been rounded to the nearest whole number unless reported otherwise.

ABOUT THE COMPANY

Promontory Interfinancial Network offers unique services that bring banks and other institutions together in a way that helps each to benefit from The Power of Many—enabling them to offer services that otherwise might be too difficult or costly to offer on their own and providing them with tools to help manage their balance sheets.

Promontory Interfinancial Network’s services include CDARS®, IND®, Insured Cash Sweep®, Yankee Sweep®, Promnet Repo®, and Bank Assetpoint®.

For more information about this survey, Promontory Interfinancial Network, or its services, please call (866) 776-6426 or visit Promnetwork.com.