Objectives

- The Regulatory Perspective
- Identifying Concentrations
- Risk Management Practices
- Supervisory Treatment
- Outstanding Guidance
What is a concentration?
Lessons Learned
Bank Failures
Level and Trend
Causes and Consequences of Recent Bank Failures

“The failures of the smaller banks (those with less than $1 billion in assets) were largely driven by credit losses on commercial real estate loans. The failed banks also had often pursued aggressive growth strategies using nontraditional, riskier funding sources and exhibited weak underwriting and credit administration practices. The rapid growth of commercial real estate portfolios led to high concentrations that increased the banks’ exposure to the sustained real estate and economic downturn that began in 2007.”

GAO-13-71, Financial Institutions: Causes and Consequences of Recent Bank Failures
Bank Failures

Nationally, over 500 institutions failed.

- Georgia, Florida, California, and Illinois had the most failures.
- Look Back Reports
  - Office of Inspector General
  - US Government Accountability Office

Chicago Region Failures from 2007 to Present

Information obtained from www.FDIC.gov
$1.8 billion institution in Michigan

- Concentrations in CRE/ADC and private label CMOs
- Increase in brokered deposits to fund growth
- 117% ADC/Total Capital; 376% CRE/Total Capital
Specific Examples from the Region*

- $1.7 billion institution in Illinois
  - Concentrations in CRE/ADC
  - Out-of-area loan participations and brokered loans
  - Volatile funding sources

*Information obtained from OIG Material Loss Reviews
What did 2015 look like?

Source: FDIC
Total Commercial Real Estate By Component

Billions

- Total CRE ($)
- Total ADC ($)
- Total Multifamily ($)
- Total Non-Farm Non-Residential ($)
- Total Owner Occupied Non-Farm Non-Residential ($)

The breakout for Owner-Occupied was not available in the Call Reports until 2008

Source: FDIC
Note: Data through December 31, 2015.
The Oil Industry Has Been Significantly Impacted By Low Prices

OSP: WTI-Cushing; OK-FOB (USD per Barrel, NSA) for US

Source: US Energy Information Administration: Petroleum Weekly Release
Percentage of Banks with One or More Types of Funding Concentrations

2011

2015

Funding Concentration: Single funding source >10% of total assets or aggregate potentially volatile funding sources > 25% of total assets.

Source: FDIC
Does my bank have concentrations?
Group Assets With Similar Risk Factors

- Industry
- Type of Collateral
- Other Common Risk Factors
- Product Line
- Repayment Source
Commercial Real Estate By Collateral Type

Owner Occupied CRE

Other Non-Owner Occupied CRE

Multifamily

Farmland

ADC

Hotel

Office

Other

Sublimits are needed.
Can 1-4 Family Residential Loans be considered a concentration?

A. Yes
B. No
Can 1-4 family residential loans be considered a concentration?

Yes, but only if the portfolio, or one or more segments, share common higher-risk characteristics such as subprime, high loan-to-value ratios, and/or nontraditional mortgages.
Can owner-occupied CRE be considered a concentration?

A. Yes
B. No
Yes. Owner occupied CRE and non-owner occupied CRE may be combined if they share similar risk characteristics, which could include geography, product line, collateral type (e.g., retail, office, industrial), or industry (e.g., energy, healthcare practices, or tourism).
Can unfunded commitments be included?

A. Yes
B. No
Are unfunded commitments included?

They can be included. The impact of unfunded commitments on risk should be considered by management and examiners.
Can loans with guarantees from the Farm Service Agency or SBA be a concentration?

A. Yes
B. No
What about loans with guarantees from the Farm Service Agency or the Small Business Association?

- Yes, they can be considered a concentration.
- Guarantees do not free the bank of responsibilities with the credit.
- Include the full balance and address the guarantee in a qualitative analysis.
Identifying Funding Concentrations

- Brokered deposits
- Large depositors
- High-rate deposits
- Internet-listing-service deposits
- Federal funds purchased
- Borrowings
- Other
Are those funding sources *automatically* considered *volatile*???
Risk Management Program

- Board and Management Oversight
- Policies, Procedures, and Risk Limits
- Management Information Systems (MIS)
- Measuring and Monitoring Systems
Risk Management Program

- Risk Stratification and Vulnerability Assessment
- Market Analysis
- Contingency Planning
Report of Examination Treatment

- A Concentrations page will be included in Reports of Examination when concentrations exceed established concentration thresholds or when examiners determine inclusion is warranted.

- Examiners may prepare a written analysis describing the concentration and management’s risk management practices.
## Asset Category Thresholds

<table>
<thead>
<tr>
<th>Threshold</th>
<th>Examples</th>
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<tbody>
<tr>
<td>$\geq 25%$ Total Capital (loans) or Tier 1 Capital (non-loans)</td>
<td>Individual borrower, Small or Interrelated group of individuals, Single repayment source with normal credit risk or greater, Individual project</td>
</tr>
<tr>
<td>$100%$ or more of Total Capital (loans) or Tier 1 Capital (non-loans)</td>
<td>Industry, Product line, Type of collateral, Short-term obligation of one financial institution or affiliated group</td>
</tr>
</tbody>
</table>
The Report of Examination Concentrations page now lists funding concentrations.
Resources

- RMS Manual of Examination Policies, Sections 3.2
- Financial Institution Letters
  - Funding and Liquidity Risk Management - Interagency Guidance (FIL-13-2010)
  - Correspondent Concentration Risks - Interagency Guidance (FIL-18-2010)
  - Managing Commercial Real Estate Concentrations in a Challenging Environment (FIL-22-2008)
  - Commercial Real Estate Lending - Joint Guidance (FIL 104-2006)
- Supervisory Insights Journal
  - Stress Testing Credit Risk at Community Banks (Summer 2012)
  - Managing Agricultural Credit Concentrations (Winter 2010)
  - Managing Commercial Real Estate Concentrations (Winter 2007)
- Directors’ Resource Center: [www.fdic.gov/resourcecenter](http://www.fdic.gov/resourcecenter)
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