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Risk Management Association

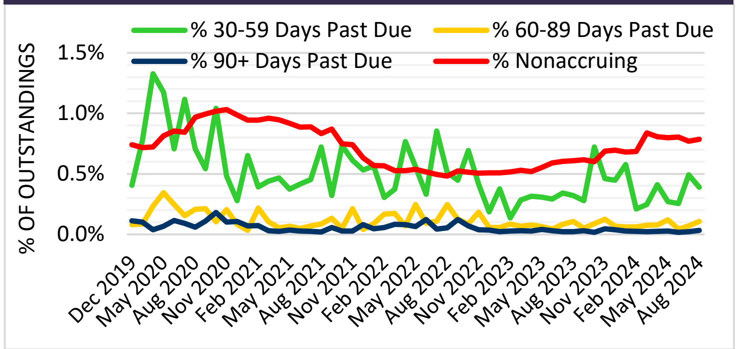
Commercial Credit Quality Bulletin

September 2024

The Fed Cuts Rates Amid Mixed Economic Signals, Providing Relief to Stressed Commercial Borrowers

As expected, the Federal Reserve slashed interest rates in September, cutting the benchmark Fed Funds Rate by half a percentage point as the focus turns from inflation to supporting the labor market. Further easing by the Fed should help improve debt-service capacity for commercial borrowers, particularly in the CRE space where criticized-rated balances were up 50% in August from the year-ago period. Higher CRE provisions could weigh on bank earnings at a time when weak commercial loan demand has hindered balance sheet growth. For C&I borrowers, nonaccruing balances plateaued in recent months, and C&I risk migration was broadly neutral as downgrades only slightly surpassed upgrades. Banks with broadly diversified loan books should fair best as markets navigate continued economic and political uncertainties.

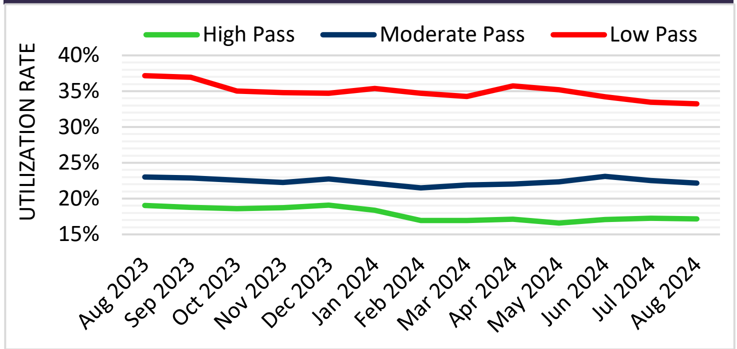
C&I Delinquency and Nonaccrual Trend



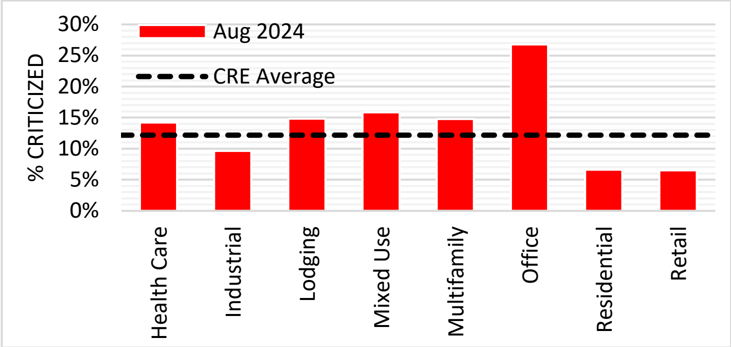
The chart on the left displays four key risk indicators for commercial and industrial (C&I) loan performance – the percentage of loan outstanding balances that are 30–59 days, 60–89 days, 90+ days past due, and loans on nonaccrual. The chart illustrates the trend in performance since year-end 2019. Nonaccruals, after increasing for most of 2023 and into early 2024, have been relatively flat over the past several months. Short-term delinquencies continue to be very volatile, especially for intra-quarter time periods. Nevertheless, the overall trend is one of improvement for key C&I loan performance indicators.

The chart on the right shows the revolving line of credit utilization (calculated as line takedowns as a percentage of the total commitment amount) over the past year. Despite the improved credit performance, loan growth has trended downward. Also of note is the overall difference in usage between the better-rated credits versus the Low Pass credits. The better-rated credits have easier access to lower cost borrowing via capital markets and are less reliant on often more expensive bank loans. Borrowers with a Low Pass credit rating have more limited financing alternatives.

C&I Revolving Line of Credit Utilization by Risk Grade



CRE Percent Criticized by Major Property Type



With the chart on the left we show the percentage of balances for borrowers that are rated Criticized (Special Mention, Substandard, Doubtful, and Loss), segmented by the eight major CRE property types. Banks typically assigned these ratings to borrowers whose prospects are less than favorable. As has been stated in past Bulletins, the outlook for Office properties is much worse than average. But surprisingly, Multifamily properties are also slightly higher than average as banks are concerned about excess supply and the lingering effect of high interest rates.

Why RMA and AFS?

RMA and AFS are committed to providing relevant, timely, and practical credit risk solutions to banks. Combining the strengths of each to offer information and insight, RMA and AFS are ideally situated for collaborations aimed at identifying and responding to the credit risk needs of financial institutions.

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