Community Depository Institution Advisory Council

Federal Reserve Bank of Dallas

Meeting Minutes

March 7, 2024

Committee Attendees:

Byron Bexley, American Bank (Council Chair)

George Cummings III, Progressive Bank

Gail Enda, American Airlines Federal Credit Union

Isaac Johnson, TDECU

Bob Malone, First Sonora Bancshares and Sonora Bank

Katherine Rodriguez, Moody National Bank

Deborah Romero, First National Bank

Raymond Rust III, Commercial Bank of Texas, N.A.

Max Villaronga, Raiz Federal Credit Union

Federal Reserve Bank of Dallas Directors in Attendance:

Robert Hulsey, American National Bank of Texas

Joe Quiroga, Texas National Bank

Federal Reserve Bank Staff in Attendance: Lorie Logan, Robert Triplett, Emily Greenwald, Rick Mase, Karel Mertens, Michael Schetzel, Alison Schmidt, Lorenzo Garza, Amy McGregor, Heidi Mitchell, Tim Stearns, Paul Wheeler, John Alexander, Amy Chapel, Stephen Clayton, Julieta Ezeiza, Gina Gadson-Richards, Ally Hoffman, Sai Nori, Jody Stanley, Jamie Garcia, Rebin Kawani, Ben Munyan, Seth Dunbar, Jose Gonzalez, Kelly Klemme, Kelly Toman, Amy Wong

Administrative:

The meeting was called to order at 1:00 PM. Bank senior leadership made introductory remarks. A member of Bank staff provided a reminder that council members should adhere to the antitrust guidelines.

Economic Conditions Update:

Ben Munyan, director of supervisory policy, discussed national and regional economic conditions. Discussion ensued on commercial real estate (CRE) and how data accounts for different classes of CRE across banks and credit unions.

Banking Conditions Update:

Emily Greenwald, senior vice president, discussed district and national banking conditions. Subsequent discussion centered on the risks and benefits offered by reciprocal deposits. Several Council members noted that they use reciprocal deposit arrangements to ensure deposit insurance for their customers. They highlighted operational risks associated with offering this service to customers and risks associated with rapid in and outflows of deposits from participants during times of market stress.

Council members were asked to share their views on the following topics as part of the roundtable discussion:

Economic Conditions:

Council members largely reported stable to positive economic conditions across the 11th District. Small business and housing-related activity remains strong in central Texas, while growth in the Rio Grande Valley has been supported by an influx of industry and government spending. Northern Louisiana and Southern New Mexico have seen modest growth in local industry. Members were split on the state of the consumer, with some reporting customers losing jobs or seeing reductions in hours, which has resulted in an increase in charge offs on auto and consumer loans. Loan demand has slowed in some regions in response to higher interest rates, while in others, it has increased slightly off of recent lows, and near the Mexican border loan growth was exceptionally strong. Participants reported increased competition for loans and challenges posed to housing by high house prices and interest rates.

Small Business Lending:

Small business lending activity across the 11th District has ebbed and flowed since the last meeting. The hospitality segment has struggled, however other small business areas appear to be adjusting to the rate environment as the new normal.

Commercial Real Estate Lending:

Council members indicated that demand for commercial real estate loans was high, but that banks were being selective based on the quality of the potential credit. Several participants noted that banks were up against lending concentration limits but were still offering attractive terms to potential borrowers. Discussion ensued over the impact that a 100-basis point decrease in 10-year rates would have on lending to the sector. Council members agreed that the impact was segment-dependent with owner-occupied credits benefitting the most while office and multifamily likely taking longer to recover.

Construction and Residential Mortgage Lending:

Construction lending activity has slowed likely due to the impact of higher interest rates. Banks are being selective on deals in this area as many are approaching loan concentration limits. Builders are constructing smaller homes due to price constraints. Home mortgage lending has slowed across the region from recent highs. Despite a desire to move, many consumers are unwilling to trade their lower mortgage rate for the higher rates the market currently offers and pay higher prices for housing. For those that are buying in this environment, they are likely doing so with the plan to refinance to a lower rate later. For consumers looking to upsize, some are deciding to renovate their homes instead of move. Some current homeowners are using the equity in their homes to fund downpayments on second homes.

Consumer Lending:

Council members indicated that demand remains surprisingly strong for auto and other consumer lending. Some institutions are increasing pricing to slow demand, they are finding captive auto finance companies' rates to be too low to compete with in the current environment. Demand for unsecured consumer lending is likely driven by consumers (particularly younger consumers early in their careers) attempting to maintain lifestyles that were previously supported by stimulus funding. Discussion ensued on how the rapid movement of interest rates has contributed to a sense of fragility among financial institutions. Regarding consumer portfolio performance, participants indicated that delinquencies and charge-offs have increased.

Agricultural Lending:

Members reported improvement in agricultural lending throughout the region. Bankers are seeing better performance by agricultural loans and an uptick of on-time payments by those previously struggling to make payments. More rain and increased commodity prices are contributing to stability in this area.

Deposits:

Retaining deposits remains a challenge for participants. In response to an increase in the cost of funds, some institutions have focused on reducing operating expenditures and gaining efficiencies elsewhere. Discussion ensued on deposit insurance. Most consumer deposits at community banks are not large enough to require a higher limit on FDIC deposit insurance coverage. Older retail customers would likely prefer a higher limit, while commercial customers are indifferent. Enhanced coverage limits would be helpful during periods of crisis. Participants raised associated concerns including how increased deposit insurance limits would be funded, how to stimulate deposit flow back into community banks, and the speed at which deposits exited banks during the nationwide banking volatility in early 2023.

Exam Procedures:
Members discussed staffing at another regulator, noting a high degree of turnover among exam staff that has led to extended exams and an increase in inexperienced examiners. Discussion ensued regarding the balance of supervisory authority between regulators' field offices and head offices in Washington, D.C. and on the appropriate balance of on- and off-site examination activity. Participants expressed a preference for on-site exams, noting that they are often more effective and efficient. Members also expressed concern over proposed changes to overdraft and interchange fee regulation. They suggested that these efforts make it hard to project future income and may lead to a reduction in personnel to lower expenses and offset lower noninterest income.

Payments:

Council members expressed support for the launch of FedNow, suggesting that it helped level the playing field with larger financial institutions in the realm of payments. Fraud and third-party service providers remain a concern. These service providers are developing tools that will allow financial institutions to connect to the FedNow service and improve customer experience.

Third Party Service Providers:

The Council was asked to share its perspectives on third-party service providers. Members discussed whether these firms have sufficient regulatory compliance experience, how banks can monitor their activities for regulatory compliance, and overall vendor management. Discussion ensued regarding concentration risk with larger third-party service providers and the benefits of a regulatory framework to govern these firms.