PMA™
FINANCIAL NETWORK

CREDIT QUARTERLY

MARCH 2019

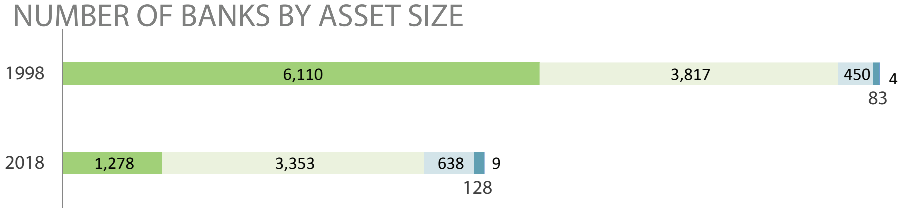
INSIDE THIS ISSUE

RECENT NEWS

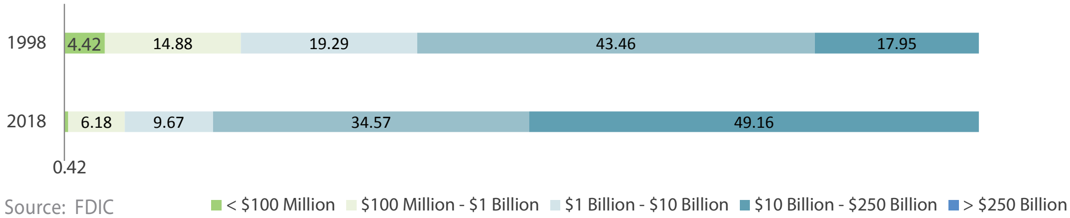
Regional Banks Agree to Merge

In February, U.S. regional lender BB&T Corp. agreed to buy SunTrust Banks Inc. for $28.2 billion in stock to create the sixth-largest U.S. retail bank. BB&T had $226 billion in assets at the end of 2018, while SunTrust had $216 billion. It is the largest U.S. bank merger since 2004 and continues the concentration of bank assets and deposits at the largest players. Banks with over $250 billion in assets now comprise almost half of total industry assets, versus 18% in 1998. Technology was the main impetus for the deal as regional lenders are struggling to compete with the big national banks, which are attracting a greater share of new checking accounts from customers drawn to their digital offerings. The banks expect the merger to close in the fourth quarter of 2019 and project it will produce approximately $1.6 billion in annual cost savings by 2022. The market and regulatory environment could force banks of similar size and smaller depositories to seek out their own deals in order to increase efficiencies in regards to regulatory and risk requirements and technology costs. Over the past twenty years, the number of banks has shrunk in half due to mergers and, to a lesser extent, bank failures.

NUMBER OF BANKS BY ASSET SIZE



SHARE OF TOTAL INDUSTRY ASSETS BY ASSET SIZE



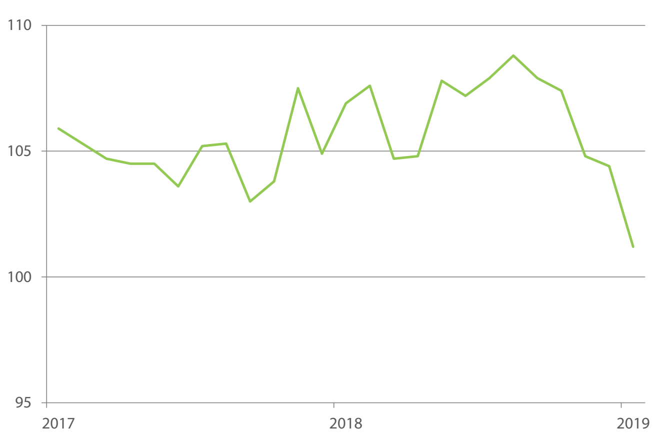
Source: FDIC

NFIB SMALL BUSINESS OPTIMISM INDEX

The Small Business Optimism Index is a composite of ten Small Business Economic Trend indicators that provides a monthly, summary data point for the state of the small business economy. It is a coincident indicator of the national economy, though it also offers direction for the small business sector's immediate prospects.

CREDIT TRENDS AND COMMENTARY

NFIB SMALL BUSINESS OPTIMISM INDEX



Source: National Federation of Independent Business (NFIB) Research Foundation

The NFIB's Small Business Optimism Index dropped to 101.2 in January 2019 from 104.4 in December. The majority of the decrease came from softer expectations for real sales growth and business conditions in the second half of 2019. Amid growing economic uncertainty, loan growth slowed at U.S. community banks during the fourth quarter of 2018.

PROBLEM INSTITUTIONS

Number of institutions on the FDIC's "Problem Bank List" for the respective year:

2018 | 60

2017 | 95

2016 | 123

2015 | 183

2014 | 291

Source: Federal Deposit Insurance Corporation (FDIC)

BANKING TRENDS

4th Quarter 2018 Highlights

FDIC-insured institutions reported fourth quarter 2018 net income of $59.1 billion, an increase of $33.8 billion (133.4%) compared with the prior year period. The significant jump was mainly driven by lower income tax expenses enacted from the new tax law and higher net operating revenue. More than 83% of banks reported year-over-year increases in net interest income. Average net interest margin increased to 3.48% from 3.31% in fourth quarter 2017. Only 6.5% of institutions were unprofitable during the quarter, nearly a 10% decline from the year prior.

Net charge-offs declined 4.6% year-over-year to $12.6 billion. This was the first time since third quarter 2015 that net charge-offs declined. Provisions for loan losses in the fourth quarter totaled $14 billion, an increase of $397 million from a year ago. Noncurrent balances for total loans and leases decreased $1 billion (1%) during the fourth quarter compared to the prior quarter. In addition, the average noncurrent rate was 0.99% during the fourth quarter, its lowest mark since second quarter 2007.

Total assets rose by $270.4 billion (1.5%) from the previous quarter. All major loan categories saw quarterly growth, with total loans and leases increasing 2.1% to $213 billion. Retained earnings jumped $70.8 billion (10.3%) from a year ago even as declared dividends rose to the highest level ever reported in the banking industry. The number of institutions on the FDIC's "Problem List "declined from 71 to 60 in the fourth quarter, the lowest number of problem banks since first quarter 2007. For full-year 2018, eight new charters were added, 259 institutions were absorbed by mergers, and zero institutions failed.

Source: FDIC Quarterly Banking Profile

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PRUDENT MAN PROCESS

The Prudent Man Analysis

The Prudent Man Process includes four steps which begin with gathering data and analyzing a bank's credit quality and continues with ongoing risk management throughout the life of a deposit. The process helps public funds investors avoid repayment, reinvestment and reputation risk that may be associated with a bank failure.

Step 1: Gather Bank Data

The process begins with gathering bank, industry and economic data from an extensive list of sources. Bank financial data is received from a variety of regulatory filings. Industry tools like Bloomberg and S&P Global Market Intelligence are utilized in obtaining data and other relevant information. Additionally, a number of publications focusing on the banking industry and local and national economy are monitored daily.

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