

FITCH WIRE

US Bank Credit Loss Reserve Coverage Reverts to Pre-Pandemic Levels

Thu 18 Nov, 2021 - 3:28 PM ET

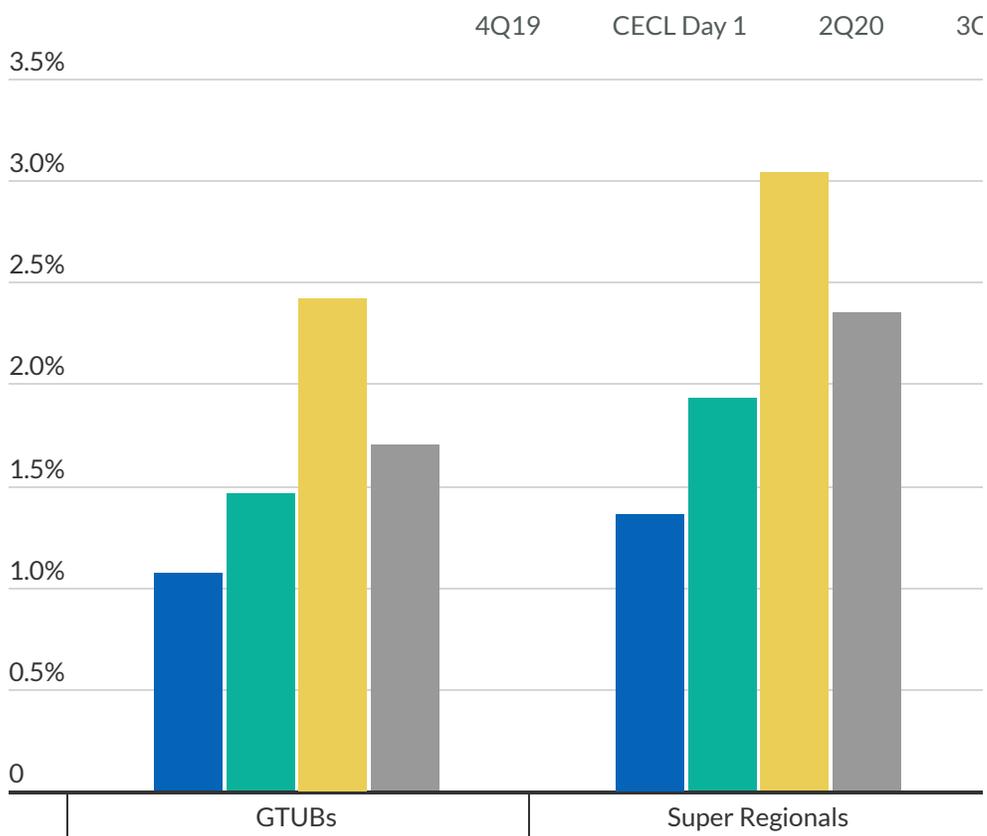
Fitch Ratings-New York/Chicago-18 November 2021: Reserve coverage for many U.S. banks is declining toward pre-pandemic Current Expected Credit Loss (CECL) Day 1 coverage levels, as the economic fallout from the global pandemic subsides and stabilizing or improving economic outlooks of the past 12-18 months are incorporated in CECL model forecasts, Fitch Ratings says. Fitch-rated banks have seen a convergence in allowance for loan losses as a percentage of total loans from peak levels in mid-2020, signaling a return to a new normal. Lower coverage ratios are typically a credit negative, but Fitch does not view the shrinking coverage levels negatively for most banks given the improving economic backdrop.

CECL coverage rates are particularly sensitive to the economic outlook as well as other considerations such as loan type, sector and geography, duration, underwriting terms and loss history. Most banks had modest increases in reserve levels upon CECL adoption on Jan. 1, 2020, but saw a steep increase in reserve coverage in early 2020 as the negative outlook from the global pandemic was incorporated into loss allowances, displaying the procyclicality of the CECL models.

Banks began to release reserves in 2H20 and early 2021 as the economy proved more stable than previously anticipated. Many banks are nearing pre-coronavirus reserve levels, signifying a somewhat stabilized economic outlook, following several quarters of releases.

U.S. Banks Allowance for Loan Loss Coverage

Pre-CECL Adoption Through 3Q21



Note: GTUBs include BAC, C, GS, JPM, MS. Super Regionals include TFC, COF, PNC, USB, WFC. Large Regionals include CFG, CMA, FHN, FITB, FRC, HBAN, KEY, MTB, RF, ZION.

Allowance coverage levels for the majority of Fitch-rated banks remain slightly above Day 1 coverage levels, apart from JP Morgan and First Republic Bank. On average, the Global Trading and Universal Banks (GTUBs), Super Regional and Large Regional Fitch-rated banks' coverage ratios remain 22 bps above Day 1 levels. Large regional banks, which had the smallest reserve coverage increase in 2020, have been the quickest to converge on Day 1 levels, only 16 bps on average above pre-pandemic coverage at 3Q21. Super regionals remain highest at 42 bps on average above Day 1 coverage.

U.S. Banks' Allowance for Loan Loss Coverage

Allowance Coverage Is Converging on CECL Day 1 Levels

Note: Allowance for loans and lease losses as a percentage of total loans. COF Excluded for Scale Purposes: CECL Day 1:

3.96%, 2Q20: 6.69%, 3Q21: 4.43%. CECL - Current expected credit loss. GTUB - Global trading and universal banks.

Source: Fitch Ratings.

The conversion to pre-pandemic coverage levels is somewhat arbitrary, as loan portfolios have changed from the CECL Day 1 pre-pandemic compositions. Additionally, while economic outlooks have generally stabilized, uncertainty remains regarding supply chain constraints, interest rate hikes, continued inflation and the impact of waning federal stimulus.

Fitch's U.S. macroeconomic forecasts as outlined in the [September 2021 Global Economic Outlook](#) show improvements in the projections for GDP, consumer spending, and fixed investment yields compared to the pre-pandemic December 2019 Fitch Global Economic Outlook. However, this is weakened by higher inflation and unemployment levels and lower net trade contribution. As such, CECL models may be producing similar allowance coverage to CECL Day 1, but the drivers of the outcome may have changed.

Fitch anticipates that allowance coverage ratios will bottom out in 4Q21 or 1Q22 and that provision expenses will begin to increase in 1H22 should lending pick up. However, the return of provision expenses is not expected to raise allowance coverage ratios meaningfully above CECL Day 1 levels. Should allowance coverage ratios fall significantly below CECL Day 1 levels, Fitch may view the diminishing coverage levels as a credit negative.

Related Research:

Oct. 15, 2021: [US Banks See 3Q Reserve Releases on Strong Credit, Tepid Loan Growth](#)

April 13, 2020: [Coronavirus Will Magnify CECL Challenges for US Lenders](#)

Oct. 29, 2019: [Financial Institutions Dashboard: CECL Impact Varies by Bank](#)

Contacts:

Lauren Young, CPA

Senior Analyst, Financial Institutions

+1 646 582-3621

Fitch Ratings, Inc.

300 West 57th Street

New York, NY 10019

Johannes Moller, CFA, FRM

Director, Financial Institutions

+1 646 582-4954

Christopher Baker

Director, financial Institutions

+1 312 606-2361

Laura Kaster, CFA

Senior Director, Fitch Wire

North and South American Financial Institutions

+1 646 582-4497

Media Relations: Sandro Scenga, New York, Tel: +1 212 908 0278, Email:

sandro.scenga@thefitchgroup.com

The above article originally appeared as a post on the Fitch Wire credit market commentary page. The original article can be accessed at www.fitchratings.com. All opinions expressed are those of Fitch Ratings.

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers.

Please read these limitations and disclaimers by following this link:

<https://www.fitchratings.com/understandingcreditratings>. In addition, the following <https://www.fitchratings.com/rating-definitions-document> details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default.

Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct section of this site. Directors and shareholders' relevant interests are available at

<https://www.fitchratings.com/site/regulatory>. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and

complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed. The information in this report is provided 'as is' without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic

subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the 'NRSRO'). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the 'non-NRSROs') and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

Copyright © 2021 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved.

Banks North America United States
