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RECENT NEWS

The Fed's Alphabet Soup

In light of the coronavirus and ensuing market volatility, the Fed has been very active with a host of policy changes and funding programs to ensure adequate liquidity and funding to the markets. Below is a summary of relevant changes.

Policy	Description
Policy rate cuts	After three 25bp cuts in 2019, the Fed cut the fed funds target range 50bp on Mar 3, then another 100bp on Mar 15, to 0.00-0.25%. IOER set to 0.10%, RRP at 0.00%.
Treasury and MBS purchases	At least \$500bn of Treasury purchases across the curve and \$200bn of MBS purchases announced on Mar 15. Increased to "the amounts needed to support smooth market functioning" with no hard limit on Mar 23. Will also buy Agency CMBS, with Blackrock advising on these transactions as well as with the PMCCF/SMCCF.
Supplementary Leverage Ratio relief	Announced Apr 1, the Fed would exclude US Treasury securities and deposits at Federal Reserve Banks from the calculation of SLR for holding companies, and will be in effect until March 31, 2021. On May 15, the Fed/FDIC/OCC jointly announced that depository institutions can choose to exclude US Treasury securities and deposits at the Federal Reserve Banks from the SLR calculation.
Discount window and reserve changes	Cut the primary credit discount window rate to 0.25% on March 15, at the top of the fed funds target range (vs. 50bp above normally). Allowed banks to borrow for up to 90 days, and encouraged banks to borrow at the discount window and utilize intraday credit to extend credit to businesses and households. Cut the 10% fractional reserve requirement to 0%.
Commercial paper funding facility (CPFF)	Announced Mar 17, will purchase A1/P1 (Tier 1) commercial paper directly from US issuers (including munis) at a rate of 3m OIS + 110bp (reduced from OIS + 200bp on Mar 23). Provides a funding backstop to issuers. \$10bn of credit protection from Treasury's Exchange Stabilization Fund (ESF). Began operation on April 14.
Money market liquidity facility (MMLF)	Announced Mar 18, MMLF provides liquidity to money market funds, by providing non-recourse loans to primary dealers to purchase eligible assets from MMFs. The Fed takes the credit risk (secured by a \$10bn backstop from the Treasury ESF), and will neutralize the impact on regulatory capital rules for participating banks. Treasuries, agencies, and Tier 1, US-issuer CP are eligible. CDs and munis were added Mar 23. Lending began on Mar 23 and will be in operation until at least Sep 30.
Primary Market Corporate Credit Facility (PMCCF)	Announced Mar 23, serves as a funding backstop for corporate debt by purchasing corporate bonds (or making loans) directly from issuers at a rate "informed by market conditions." US businesses rated BBB or above are eligible, except those that are "expected to receive direct financial assistance under pending federal legislation." On Apr 9, the Treasury ESF equity investment was increased to \$50bn and the combined size of the Facility and the SMCCF also increased to up to \$750bn in total.
Secondary Market Corporate Credit Facility (SMCCF)	Announced Mar 23, will purchase corporate bonds and corporate bond ETFs directly in the secondary market (at fair market value). Eligible bonds must be issued by the same issuers eligible for the PMCCF (BBB-or above, etc.) and can have a maximum maturity of 5 years. ETFs must be US listed and must aim to provide broad exposure to the US IG corporate market. Will buy no more than 10% of an issuer's max bonds outstanding over the past year, and no more than 20% of a particular ETF. \$10bn equity investment from the Treasury ESF. Operations have begun for ETF purchases and individual bonds.

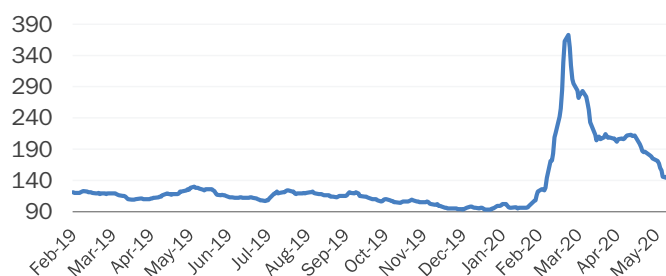
Source: S&P Global Market Intelligence

S&P RATING CHANGES

The average option adjusted spread, as measured against U.S. Treasury bonds according to the Bloomberg Barclays U.S. Investment Grade Corporate Bond Index.

CREDIT TRENDS AND COMMENTARY

BLOOMBERG BARCLAYS US AGG CORPORATE OAS



Source: Bloomberg

In June, spreads for investment grade corporate bonds tightened to 147 basis points from a peak of 372 basis points in March 2020 as investor confidence was largely restored. However, it's unlikely that spreads reestablish tightness beyond pre-pandemic levels without a prolonged period of low volatility. New issue volume is running 97% ahead of last year's pace and has eclipsed 2019 gross supply.

BANK FAILURES

Number of failed institutions
for the respective year:

2020		1
2019		4
2018		0
2017		8
2016		5

Source: Federal Deposit
Insurance Corporation (FDIC)

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BANKING TRENDS

1st Quarter 2020 Highlights

FDIC-insured institutions reported first quarter 2020 net income of \$18.5 billion, a decrease of \$42.2 billion (69.6%) compared with the prior year period. The annual decline is a reflection of deteriorating economic activity, which resulted in an increase in provision expenses and goodwill impairment charges. Slightly more than half (55.9%) of all banks reported year-over-year declines in net income, and the percentage of unprofitable banks in the first quarter increased from a year ago to 7.3%. Average net interest margin (NIM) was down 29 basis points from a year ago to 3.13%, as the decline in average earning asset yields outpaced the decline in average funding costs.

Provisions for credit losses in the fourth quarter totaled \$52.7 billion, an increase of \$38.8 billion from a year ago. Almost half (49.9%) of all banks reported year-over-year increases in loan-loss provisions. Noncurrent balances for total loans and leases increased \$7 billion (7.30%) during the first quarter compared to the prior quarter, the highest quarterly dollar increase since first quarter 2010. The average net charge-off rate increased five basis points from a year earlier to 0.55%, driven by increases in commercial and industrial and credit card loans.

Total assets rose by \$1.6 trillion (8.6%) from the previous quarter. Almost all of the major loan categories registered quarterly increases, except for the credit card balances which declined by \$68.6 billion (7.3%). Total equity capital increased by \$4.2 billion from the previous quarter. Declared dividends in the first quarter totaled \$32.7 billion, exceeding the quarterly net income of \$18.5 billion, and resulting in a \$14.2 billion reduction of retained earnings. The number of institutions on the FDIC's "Problem List" increased from 51 to 54 in the first quarter. During the quarter, two new charters were added, 57 institutions were absorbed by mergers, and one institution failed.

Source: FDIC Quarterly Banking Profile

THE PMA REPORT

The PMA Credit Research Process

The PMA 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 2: Data Analysis – Qualitative

Bank credit analysis requires insight into a bank's balance sheet, management and regulatory standing. The composition and quality of assets and liabilities are reviewed, as any balance sheet concentrations can provide insight into a bank's risk profile. To determine regulatory standing, analysts search for bank enforcement actions on the FDIC, OCC and Federal Reserve Bank websites. Additionally, if the company is publicly traded, a review of public Securities and Exchange Commission documents is completed.

Qualitative analysis also includes an assessment of industry performance and economic conditions. Banking industry developments are monitored daily and analysts conduct sector analysis within the banking industry to better understand business segments such as commercial real estate, residential mortgages and credit card lending. Economic trends that may affect bank performance are also monitored.

Financial Strategies for Stronger Communities.™

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