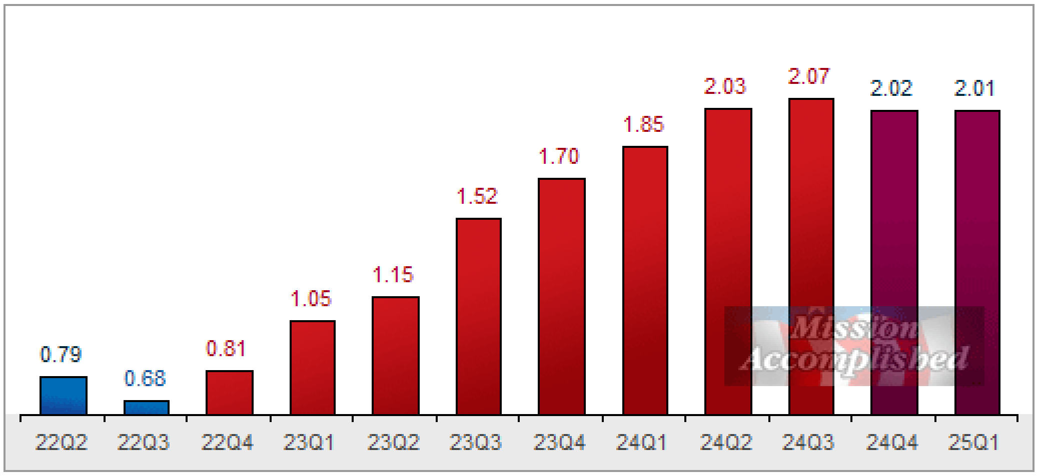
NON OCCUPIED CRE DELINQUENCIES

Bank Non Owner CRE delinquencies have moderated the past few quarters dropping from a peak 2.07% in 2024 Q3 to 2.01% in 2025 Q1. Non Owner CRE are commercial real estate loans being paid back from rental income.

Non Owner Delinquency Rate: All US Banks



On the surface, this looks like potentially great news. The problem is that it is fake. It's an entirely managed figure by the larger banks to provide the illusion that their CRE portfolios are curing.

There are four primary ways delinquencies come down:
1) Borrower pays past due amount and pays moving forward
2) Bank modifies loan to lower payment helping avoid future delinquency
3) Bank sells the loan (either completely, bank-funded or other-bank-funded)
4) Bank charges the loan off

The combination of these four have to be larger than incoming new delinquencies.

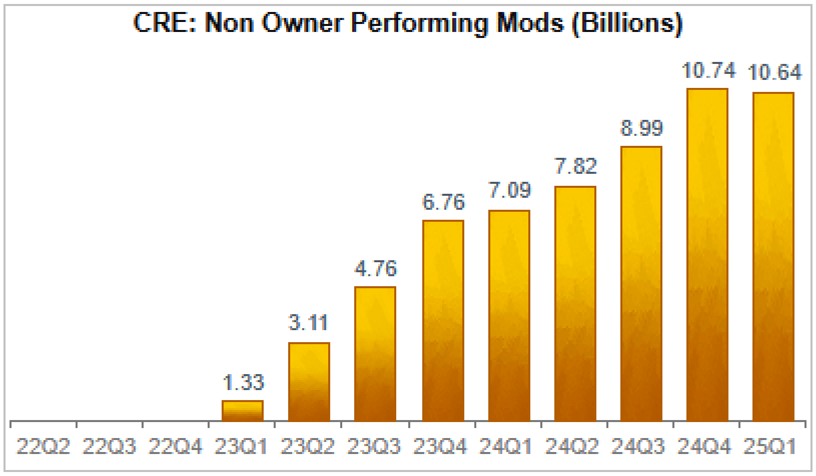
Charge offs have certainly been elevated recently, but not enough to be the main driver. The primary drivers are Loan Modifications (which we can measure) and Loan Sales (which are currently near impossible to measure).

Loan Sales come in a variety of methods on the continuum from fantastic solution to little more than loan laundering temporarily removing it from a bank's balance sheet. Without the ability to track in the Call Report the amount of money lent to fund loan acquisitions (by portfolio preferably) we have little understanding of what CRE exposure banks continue to have.

What is measurable is loan modifications. Driven almost entirely by the larger banks, it's clear the industry is modifying Non Owner CRE loans at an unprecedented pace. Lower enough payments you'll eventually see your delinquencies drop.

Non Owner CRE Loan Mods Left Off Nonaccrual: All US Banks

Qtr	Performing	Perc
22Q2		
22Q3		
22Q4		
23Q1	1,331,949,000	0.12
23Q2	3,112,905,000	0.27
23Q3	4,757,846,000	0.41
23Q4	6,763,043,000	0.58
24Q1	7,086,856,000	0.60
24Q2	7,818,630,000	0.67
24Q3	8,993,249,000	0.77
24Q4	10,743,026,000	0.92
25Q1	10,644,652,000	0.91



Starting with the 2023 Q1 'refresh' when banks were allowed to remove significant prior loan mods off the call report we see that Non Owner CRE Mods Left Off Nonaccrual (i.e. Extend & Pretend) has increased from $1.33 Billion (0.12% of loans) to $10.64B (0.91%).

Banks lower payments to avoid delinquencies. Done with moderation it can be an effective tool to manage select borrowers. The problem is it's a Gateway Drug that once a bank slips into loan mod mode it then becomes easier and easier to justify more and more modifications.

The next table shows Q1 Non Owner delinquencies and modifications by Asset Size.

2025 Q1 Non Owner Delinquencies & Modifications by Asset Size: All US Banks

Asset Size	NOO CRE Loans	Total Delq	Delq %	Perf TDR	pTDR %	stress %
>1 Trillion	140,698,000,000	7,369,000,000	5.24	3,511,000,000	2.50	7.73
100-999 B	183,858,503,000	7,057,925,000	3.84	3,830,698,000	2.08	5.92
50-99 B	144,522,282,000	2,355,689,000	1.63	961,364,000	0.67	2.30
5-49 B	373,945,540,000	3,390,911,000	0.91	2,099,135,000	0.56	1.47
1-4.9 B	224,136,623,000	2,196,727,000	0.98	217,830,000	0.10	1.08
500-999 M	65,167,484,000	739,945,000	1.14	15,834,000	0.02	1.16
250-499 M	29,409,005,000	369,549,000	1.26	7,514,000	0.03	1.28
0-249 M	13,056,503,000	190,026,000	1.46	1,277,000	0.01	1.47
	1,174,793,940,000	**23,669,772,000**	**2.01**	**10,644,652,000**	**0.91**	**2.92**

A ton to see here but first review the distribution of Non Owner CRE by Asset Size. Note how much Non Owner CRE is held by sub-$50 Billion banks. Second, note the biggest delinquency and modifications levels are in the largest banks.

The 4 largest banks in the top row have $140.70 Billion of Non Owner CRE loans, have a 5.24% delinquency rate and have modified another 2.50% by lowering payments and keeping them on Accrual (recognizing fee & interest income on a loan they had to lower the payment on to keep it current). Note the $7.37B Delinquency figure and the 3.51B of Performing TDR - these are unheard of levels of modifications.

These are mutually exclusive buckets of risk and so can be added together. The 4 largest banks have 7.73% of their Non Owner portfolio either delinquent or modified to avoid delinquencies. Wells Fargo is at 8.37% and Bank of America at 10.97%.

It's clear that banks above $100 Billion in assets are using Loan Modifications at extremely high levels. We're also seeing the banks in the $5-99 Billion range start ramping up loan modifications.

The banks below $5 Billion have virtually no Performing TDR. This means they either have very low modifications or when they do lower payments they are correctly putting the loan on Nonaccrual so that it shows up as a delinquency.

So, the big question is whether these unprecedented levels of large bank CRE Loan Modifications with solve the CRE problem?

I'm doubtful as history shows that loan modifications at best delay the increase in delinquencies. Certainly, in individual situations there are borrowers who will cure and pay out the remainder of the loan. As a pool, however, the 18-24 month charge off rate on modifications is considerably higher than the base portfolio. There is a reason loan modifications left off nonaccrual are part of the Texas Ratio.

I'm also doubtful this will serve as a solution since we're seeing delinquencies across all portfolios rise in concert. If we just had a CRE issue, then perhaps, but when C&I, Consumer, Multifamily and Construction all have increasing delinquencies then it's hard to see how CRE won't be further affected.

Even within Non Owner we're seeing increasing delinquencies across all asset size *except* those that are modifying at historically high levels.

Non Owner Delinquency Rate by Asset Size: All US Banks

Asset Size	23Q2	23Q3	23Q4	24Q1	24Q2	24Q3	24Q4	25Q1
>1 Trillion	2.38	4.02	4.68	4.93	5.33	**5.43**	5.39	5.24
100-999 Billion	2.76	3.26	3.61	3.99	**4.63**	4.62	4.19	3.84
50-99 Billion	0.45	0.67	0.77	0.93	1.05	1.14	1.21	**1.63**
5-49 Billion	0.46	0.59	0.60	0.68	0.73	0.80	0.88	**0.91**
1-4.9 Billion	0.47	0.54	0.66	0.69	0.76	0.87	0.92	**0.98**
500-999 Million	0.57	0.65	0.77	0.91	1.00	0.99	1.03	**1.14**
250-499 Million	0.69	0.73	0.68	0.98	0.95	1.11	1.11	**1.26**
0-249 Million	0.71	0.77	0.97	1.16	1.11	1.14	1.34	**1.46**
	1.15	**1.52**	**1.70**	**1.85**	**2.03**	**2.07**	**2.02**	**2.01**

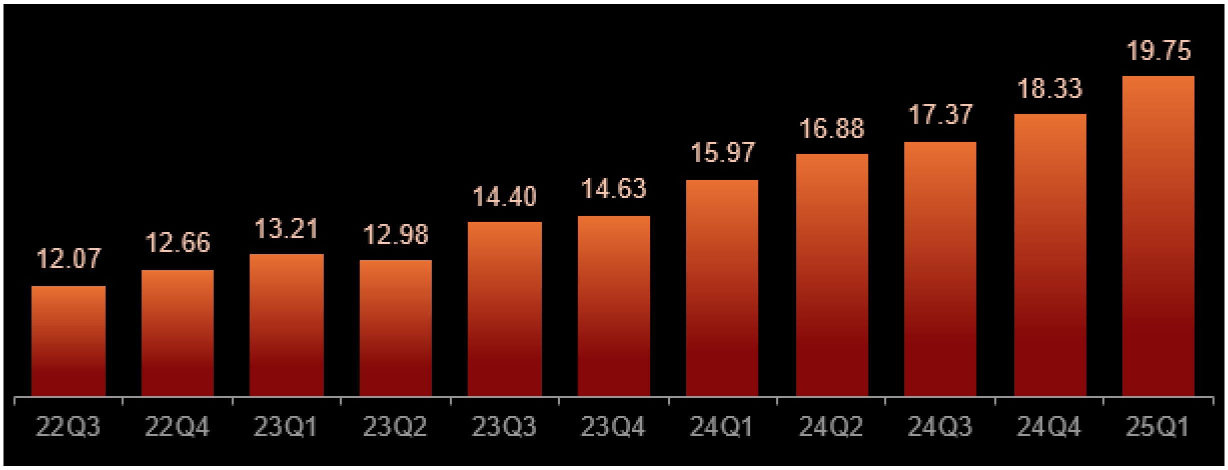
The largest banks peaked at 5.43% delinquency rate in 2024 Q3 while the $100-999 Billion banks peaked at 4.63% a quarter earlier. These are the banks that went full on Loan Modification starting early 2024. All at the exact same time almost as if they were all working from the same playbook. Surely a coincidence.

Every other asset size (even the late to the loan mod party $5-99B groups) is sitting at recent cycle highs on Non Owner Delinquencies.

This was the pattern during the GFC - the largest banks have the issues first and then, as time goes by, the delinquencies begin to increase across all asset sizes. Certainly not every bank is going to have problems, but the table clearly shows the CRE issues are spreading.

Another way to look at 'contagion' risks is to measure the % of banks having elevated delinquencies across time. The next chart tracks what percent of banks with Non Owner CRE portfolios have a delinquency rate in excess of 2.00%.

% of Banks w/ Non Owner CRE Delq Rate > 2.00%: All US Banks



This is not a weighted figure, it purely measures what portion of the industry is showing elevated delinquency stress.

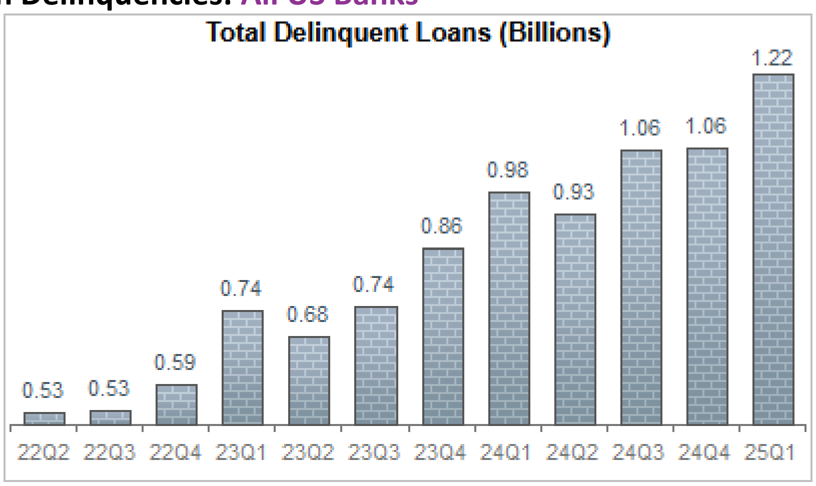
We've gone from 1 in 8 banks having issues to 1 in 5. I think it's likely we'll be 1 in 4 by the end of the year.

1-4 Family Construction Delinquencies

Industry 1-4 Construction delinquencies leapt 16bp to 1.35% in 2025 q1.

1-4 Family Construction Delinquencies: All US Banks

Qtr	Total Delinquent	Perc
22Q2	529,310,000	0.54
22Q3	532,840,000	0.52
22Q4	586,206,000	0.56
23Q1	736,314,000	0.70
23Q2	681,869,000	0.67
23Q3	744,773,000	0.75
23Q4	860,258,000	0.89
24Q1	978,458,000	1.03
24Q2	930,129,000	1.02
24Q3	1,062,884,000	1.17
24Q4	1,064,668,000	1.19
25Q1	1,217,942,000	1.35

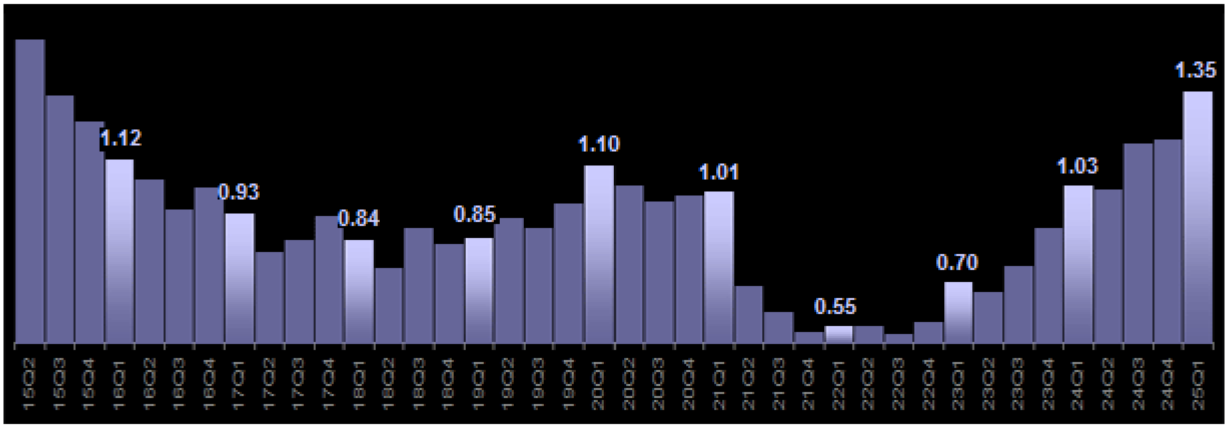


The 16bp Q on Q increase was the largest since the GFC and the industry 1.35% is the highest since 2015 Q2.

The chart is alarming, however, it's important to remember that nearly all metrics/charts that include data from 2021 and 2022 will look skewed due to the massive increase in lending during that time (artificially lowering delinquency rates) combined with the gargantuan stimulus and aid during this time (allowing consumers/businesses the ability to pay debt).

That said, the 'rebound' during the past few quarters has bounced us well above pre-Covid delinquencies.

10-Year 1-4 Family Construction Delinquencies: All US Banks



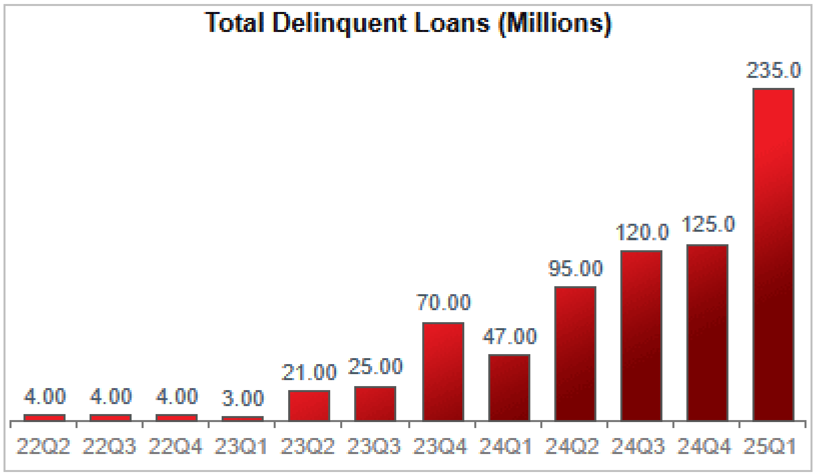
It's clear looking at the chart that the 2021 through 2022 period was well out of pattern and historically not sustainable. It's also clear that much of the current malaise is due to excessive lending that took place during that time frame as banks had to 'do something' with the extra $5 Trillion in deposits that flooded the system during 2020-2022.

The banks that went primarily with Securities purchases experienced issues in 2023 with rate normalization while the banks that lent aggressively are having an echo of delinquencies in 2024 and 2025. That's not to say all banks are/will have issues, but fast loan growth increases later delinquency risk.

A good portion of the industry 1-4 Family Construction deterioration is from JPMorgan Chase who saw delinquencies skyrocket $110 Million bringing their delinquency rate to a staggering 8.94%.

1-4 Family Construction Delinquencies: JPMorgan Chase

Qtr	Total Delinquent	Perc
22Q2	4,000,000	0.35
22Q3	4,000,000	0.50
22Q4	4,000,000	0.51
23Q1	3,000,000	0.37
23Q2	21,000,000	0.79
23Q3	25,000,000	0.88
23Q4	70,000,000	2.34
24Q1	47,000,000	1.61
24Q2	95,000,000	3.43
24Q3	120,000,000	4.18
24Q4	125,000,000	4.71
25Q1	235,000,000	8.94

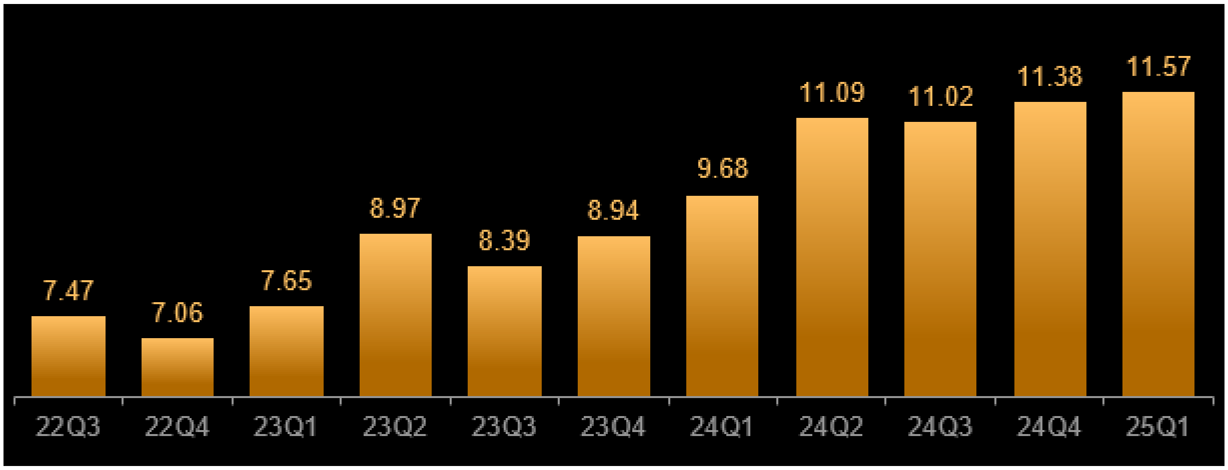


Two years ago, JPM had $3 Million in delinquencies and a 0.37% delinquency rate. That was the last quarter before the First Republic acquisition. Combined 2023 Q2 portfolio increased to $21 Million and 0.79%. I suspect that most JPM issues are likely from the First Republic legacy portfolio.

JPMorgan Chase is the second largest lender in the 1-4 Family Construction space behind U.S. Bank (which is also experiencing increasing delinquencies and loan modifications).

Similar to the earlier Non Owner chart the next exhibit shows that 1-4 Family delinquencies are spreading across a number of banks.

% of Banks w/ 1-4 Family Construction Delq Rate > 2.00%: All US Banks



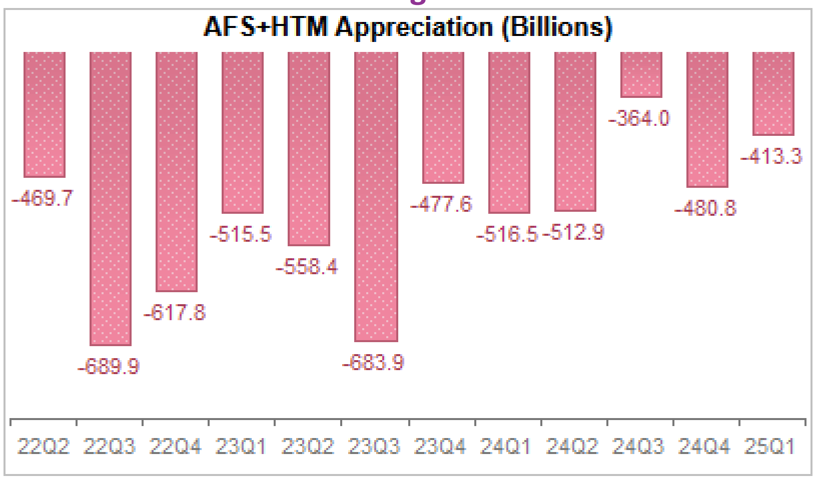
The 11.57% for 2025 Q1 is the highest since the 13.48% posted in 2014 Q3.

Securities Mark to Market Losses

With rates up 20-25bp above the March 31st Call Report, I've seen many iterations of the following chart floating around stating banks are very much still at risk.

AFS/HTM Securities Mark to Market Losses: JPMorgan Chase

Qtr	Total Appr (Dep)	Perc
22Q2	-469,677,354,000	-7.38
22Q3	-689,893,338,000	-11.07
22Q4	-617,759,805,000	-10.04
23Q1	-515,540,884,000	-8.84
23Q2	-558,424,303,000	-9.84
23Q3	-683,910,713,000	-12.24
23Q4	-477,582,472,000	-8.48
24Q1	-516,520,325,000	-9.10
24Q2	-512,919,517,000	-9.08
24Q3	-364,048,271,000	-6.40
24Q4	-480,768,511,000	-8.35
25Q1	-413,259,674,000	-7.20



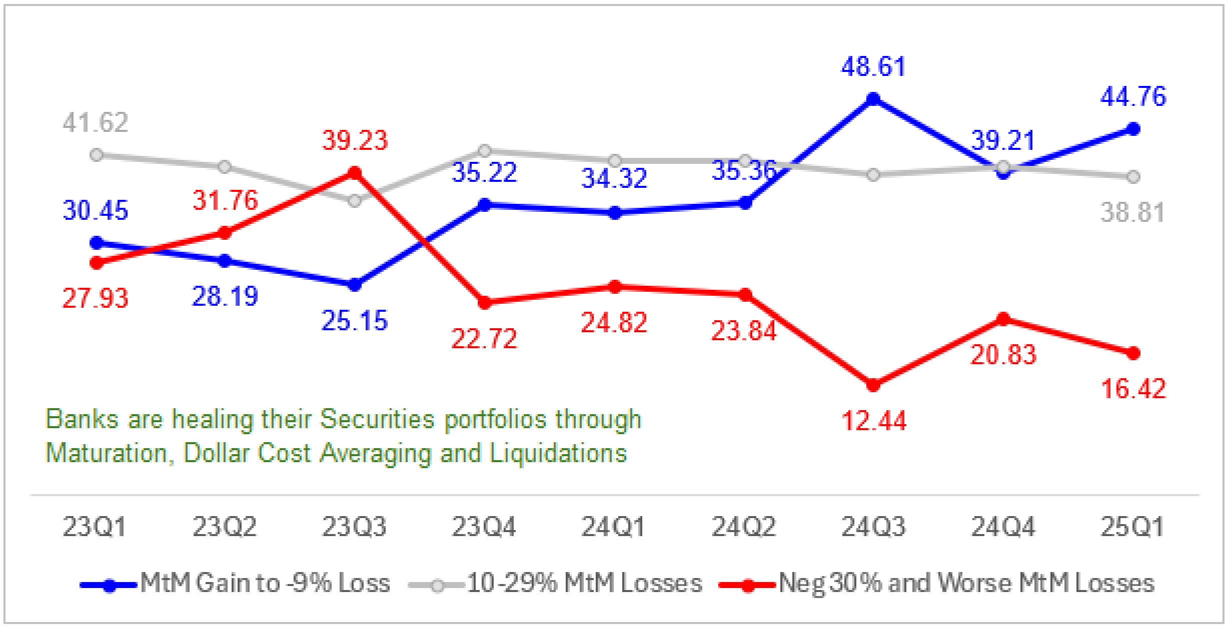
The Appreciation/Depreciation column is the amount banks are underwater on their Securities if they had to liquidate their entire portfolio. To be sure, the $413.26B loss figure (7.20% of their book) is disturbing and will likely be a good bit higher if rates stay elevated come June 30th.

That said, given rising delinquencies and loan modifications, I'm much more worried about Credit Issues than Mark to Market Securities losses. The reason is simple - banks are healing their Securities portfolios at a fairly quick pace.

I rarely advise our clients to focus on portfolio paper losses (the -7.20% industry number above). The figure I'm much more worried about is MtM Losses to Tier 1 Capital. What I watch for is the worst case scenario where complete securities liquidation would drive the bank's Tier 1 Capital below 10%.

The following chart tracks what % of banks have as losses to a percentage of capital.

Securities MtM Losses as a % to Tier 1 Capital: All US Banks



The red line indicates the % of banks that have Mark to Market Securities loss to Tier 1 Capital in excess of 30%. In 2023 Q3 nearly 40% of all U.S. Banks had losses in excess of 30% of their capital. That figure has dropped to just 16.42% today (likely to rise in Q2).

The blue line is the share of banks that have absolutely no chance of failing if they had to liquidate their securities portfolio. From just 25% in 2023 Q3 to 45% today. This is astoundingly good news.

Banks are healing their Securities portfolio through Maturation, Dollar Cost Averaging and Realized Liquidations.

The one thing that I worry about with Mark to Market losses are those banks that intersect large paper losses to capital combined with a deteriorating delinquency rate.

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