COVID-19 Insights

risk management pandemic

Summary: We explain how to incorporate the impact of COVID-19 on your borrowers into your quarterly financial statements.

You may have heard that ravens in captivity can actually be trained to speak better than parrots. That said, they may not be as fun to live with.

You have likely also heard that the Federal Reserve and the FDIC are permitting 30-day grace periods for FR Y-9C and Call Reports. It's great that the regulators have listened to bankers. If you're like us, you'd prefer not to use the grace period and have as much normalcy as possible. But each institution needs to do what it needs to do.

For those of you who are finalizing your financial statements, I'm sure you have been thinking about how COVID-19 and the resulting stay-at-home orders are affecting your borrowers and their ability to meet their financial commitments to you. Guidance states that Management should consider current economic conditions that may cause estimated credit losses to differ from historical loss experience. Therefore, it is prudent to incorporate the impact of COVID-19 in the evaluation of the adequacy of the Allowance for Loan and Lease Losses (ALLL) or Allowance for Credit Loss (ACL).

As with every new situation, there are patterns in history that can help us begin to understand our future. Looking at the historical relationship between loss rates and the economy provides a reasonable starting point to qualify the impact of COVID-19. Regression analysis is a commonly used tool to quantify this relationship. PCBB has been using this regression tool with historical data from various US government sources, publicly respected private-sector sources, and loan loss data.

Before calculated loss rates can be used in estimated loss reserves, several items should be considered. When comparing resulting calculated loss rates to your institution's loss rates, one should consider all of the unique customer segments that your institution supports and their behavior. Have your borrower's businesses been deemed non-essential, such as hotels and restaurants or essential, such as toilet paper production? Are your borrowers applying to and receiving funds from the CARES Act Paycheck Protection Program? Are your customers educators or health care workers? How will the new FMLA benefits or stimulus checks impact your community? Are there other direct and indirect impacts on your institution's loan performance from the US government's actions? How will interim modifications made today impact current or longer-term performance? What are the long-term considerations to your portfolio, such as an increased comfort with the technology supporting remote workspaces and supply chain delivery?

How your situation relates to the national data deserves a focused conversation. With everything else going on, PCBB is happy to help you with this discussion to get clarity around these types of questions. If you would like to see the analysis run for your institution using COVID-19 Insights, learn more today.

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