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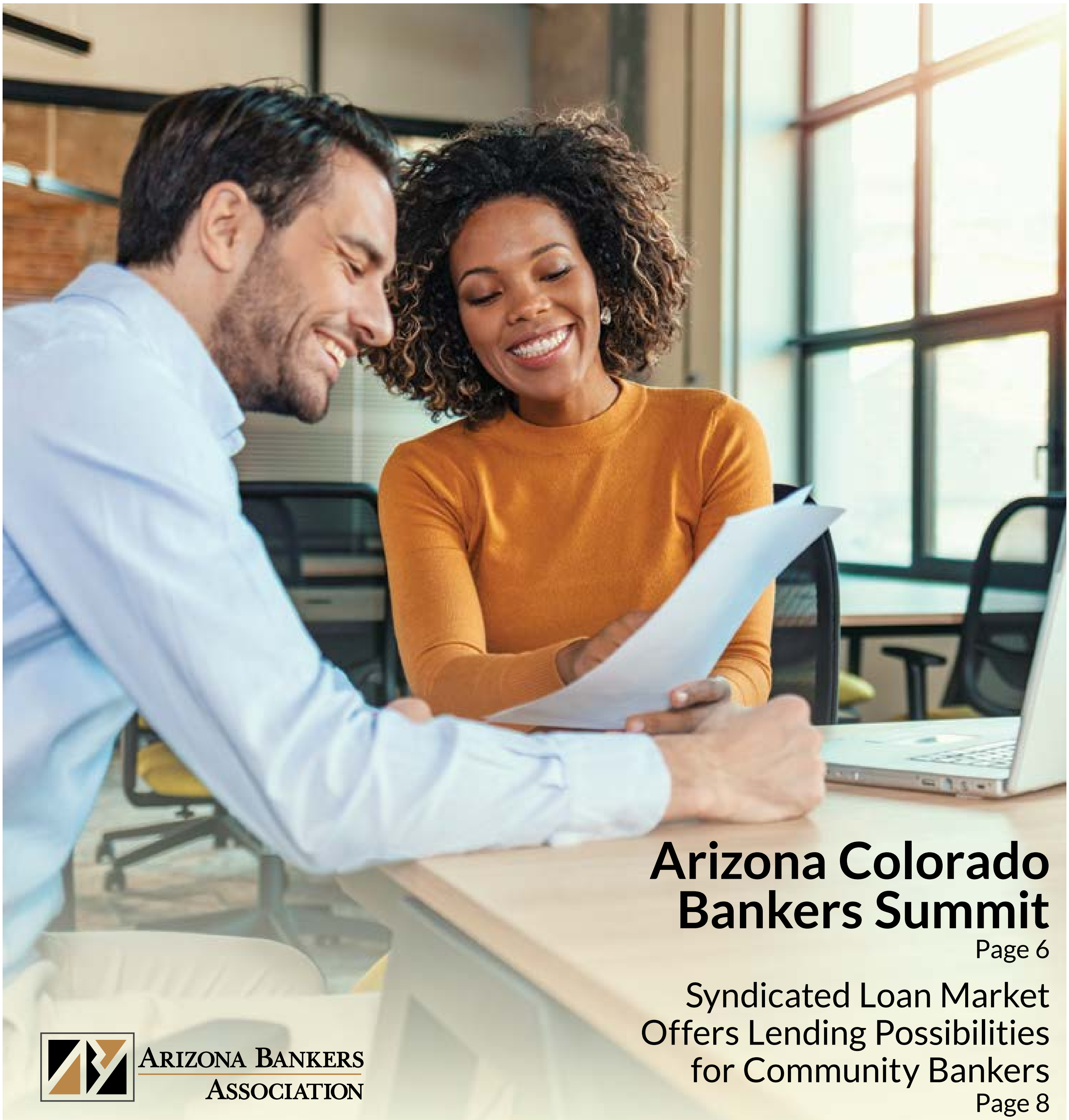

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Syndicated Loan Market Offers Lending Possibilities for Community Bankers

By Jay Kenney, PCBB SVP & Southwest Regional Manager

Many bankers are looking for ways to put their liquidity to good use. Buoyed by government relief, deposits surged at many financial institutions (FIs) at the start of the pandemic. Despite predictions that liquidity would tighten in pace with an economic recovery, FIs still have more cash than opportunities to profitably deploy it.

Net interest margins reached record lows in Q1 2021, according to S&P Global Market Intelligence, and dipped even lower in Q2. For the banking industry as a whole, aggregate taxable equivalent net interest margin dropped 2.47% in Q2, or 6bp less than Q1 and 27bp less than Q2.

With few other places to invest their cash, FIs are buying U.S. government bonds at record levels. According to JPMorgan Chase, banks purchased a record of about $150 billion in Treasury bonds in Q2 of this year. That has helped put downward pressure on bond yields.

Given the choice, however, community banks would much rather write quality loans. So, the syndicated loan market for commercial and industrial (C&I) loans may offer a place to do just that and provide an attractive option for all that liquidity.

What are syndicated C&I loans?

The $1.5 trillion syndicated loan market for secured commercial and industrial loans typically involves sizeable loans and large borrowers financing substantial transactions, such as mergers and acquisitions.

- **Strong cash flows.** Because borrowers are usually national or large regional enterprises, they have some income diversity, translating to strong cash flows.
- **Who is included?** Big banks typically originate the loans and set their terms, then pull together other lenders that complete the deal as a group.
- **Floating rates.** Rates usually float at points over an index; that used to be LIBOR, though the index choice is gradually becoming more diverse.
- **Short terms.** Loan terms are five to seven years, and the debt amortizes wholly or in part.
- **High liquidity.** Lenders typically have a first lien on assets – an important detail, especially considering that borrowers are often heavily leveraged. Running the gamut from low to high risk and corresponding returns, all these loans trade in a secondary market, making them liquid.

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How community banks can benefit?

Through years of experience in this market, PCBB has found the following advantages with syndicated C&I loans.

- **Flexibility.** The liquidity is one potential benefit to owning a piece of one of these loans. An FI that buys a loan from another FI in most other situations might be able to exit the position, but only by selling the loan back to the originator. If the first institution doesn't want to repurchase the loan, the second one is stuck. These C&I loans offer quicker liquidity and more flexibility.

- **Interest income and diversification.** Syndicated C&I loans generally offer returns that, on a risk-adjusted basis, compare well with a C&I portfolio based in a small, local market. Returns are particularly good given the current low-rate environment. With a variety of borrowers in various industries, these loans allow you to use your liquidity and diversify your loan portfolio at the same time.

Moreover, this kind of lending offers small community banks an opportunity for loan growth that in the past has been the domain of large banks. Given the current challenges for many community banks to expand their lending, they may want to look into the syndicated C&I debt marketplace. ◗

PCBB has a C&I program that can increase your loan portfolio. To learn more, please contact Jay Kenney at pcbb.com or jkenney@pcbb.com.