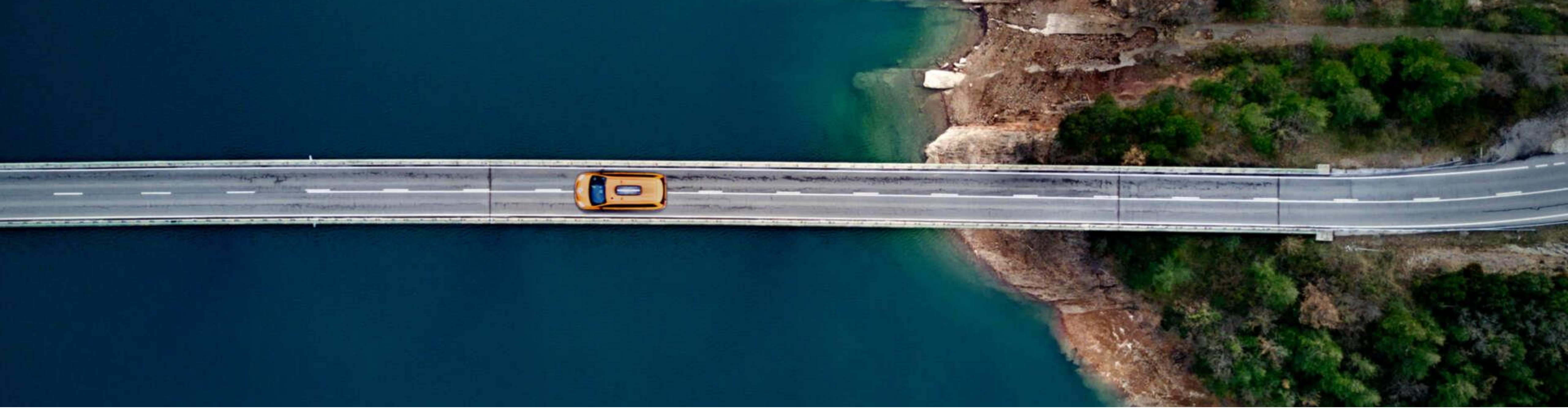


U.S. Bank Outlook 2025

Entering A New Phase Under A New Administration

Devi Aurora

Stuart Plesser

Brendan Browne

Jan. 14, 2025

S&P Global Ratings

This report does not constitute a rating action

Key Takeaways

Key expectations

- The U.S. banking industry has performed well after rebounding from 2023’s large failures and should generate relatively good earnings in 2025.
- The economy will likely grow about 2%, but with a potential for greater-than-anticipated inflation and rates in the near term, and slower growth in the medium term amid uncertainty about how much of President-elect Trump's campaign promises will materialize.
- Regulators will likely continue working on changes to capital, liquidity, stress testing, and resolution rules, but the direction may change materially depending on the Trump administration's regulatory appointments and general stance on regulation.

Key assumptions

- Incremental rises in expenses and provisions may offset growth of net interest income and fee income. Overall, we expect banks to generate a return on common equity of 10.5%-11.5% in 2025 versus a projected 11.0%-11.5% in 2024.
- The Federal Reserve will reduce rates gradually, but the probability of significant rate cuts has fallen. Long-term rates will likely decline less than the Fed’s target rate, which may support NIM but hurt loan growth.
- While the probability of significant regulatory tightening will decline materially with new appointments to regulatory bodies, existing key prudential regulations, particularly on the largest banks, will not be materially weakened.

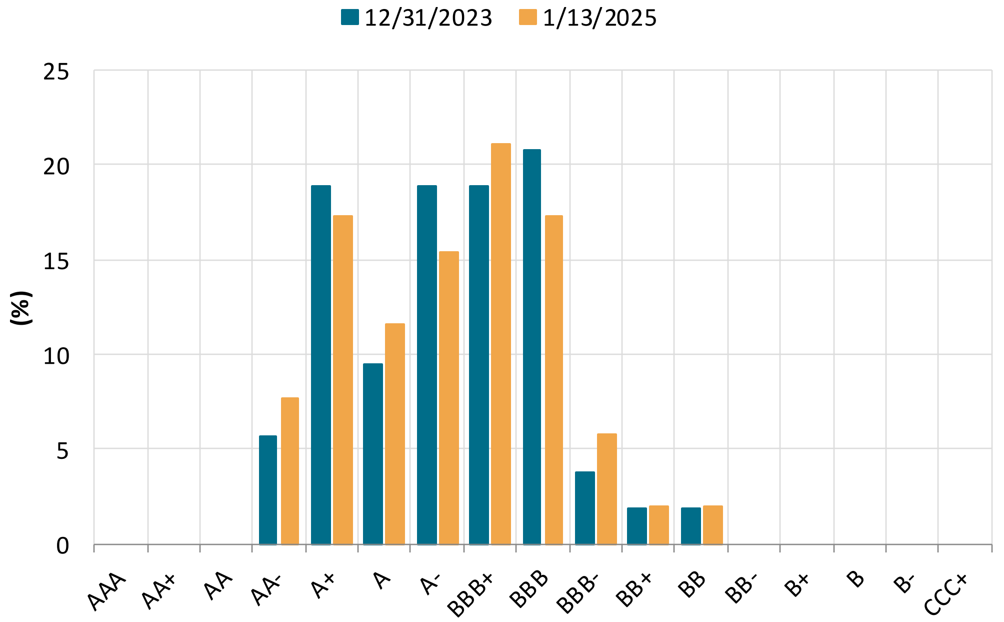
Key risks

- The economy slows materially, inflation remains high, global trading partners retaliate to tariffs, and market valuations post sharp declines.
- Long-term rates remain high or increase, adding to unrealized losses on banks’ securities and pressuring asset quality.
- The substance and tone of prudential bank regulation eases more than we anticipate, allowing for greater risk taking.
- Private credit and nonbank credit intermediation in general continue to grow materially, adding to systemic risk.

U.S. Bank Rating Outlooks Remain Largely Stable

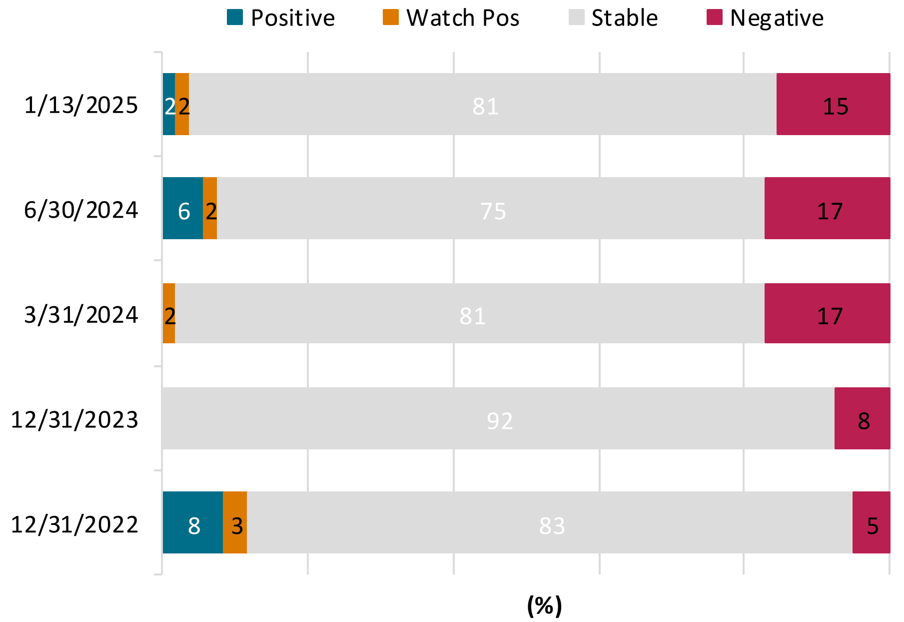
- While most banks remain on stable outlooks, reflecting continued good performance, the proportion of negative outlooks rose last year, partly due to commercial real estate (CRE) challenges and other risks. We will continue to assess those risks as they evolve.
- There were also some positive actions in 2024. We raised our rating on JPMorgan Chase and American Express and revised our outlook on OFG Bancorp to positive. We also placed Discover on CreditWatch positive after it agreed to be acquired by Capital One.

Operating company rating distribution



Note: Includes banks domiciled in Puerto Rico. Data as of January 13, 2025. Source: S&P Global Ratings.

Outlook distribution



Note: Includes banks domiciled in Puerto Rico. Data as of January 13, 2025. Source: S&P Global Ratings.

U.S. Economic Outlook

S&P Global U.S. economic forecast overview

November 2024

Key indicator (year % change)	2020	2021	2022	2023	2024f	2025f	2026f	2027f
Real GDP	-2.2	6.1	2.5	2.9	2.7	2.0	2.0	1.7
Real consumer spending	-2.5	8.8	3.0	2.5	2.6	2.3	2.0	2.3
Real equipment investment	-10.1	6.7	4.4	3.5	3.7	4.2	4.3	2.8
Real nonresidential structures investment	-9.2	-2.6	3.6	10.8	3.4	0.1	2.4	0.3
Real residential investment	7.7	10.9	-8.6	-8.3	3.9	0.8	2.6	2.2
Core CPI	1.7	3.6	6.2	4.8	3.4	2.6	2.4	2.3
Unemployment rate (%)	8.1	5.4	3.7	3.6	4.0	4.2	4.2	3.9
Housing starts (annual total in mil.)	1.4	1.6	1.6	1.4	1.4	1.4	1.4	1.5
10-Year Treasury (%)	0.9	1.4	3.0	4.0	4.2	4.0	3.6	3.6

Note: All percentages are annual averages, unless otherwise noted. Core CPI is the Consumer Price Index excluding energy and food components. f--forecast. Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve, Oxford Economics, and S&P Global Economics' forecasts.

- We forecast the U.S. economy to expand 2.0% in the next two years--incorporating partial implementation of Trump's proposed policies—following an estimated 2.7% growth in 2024.
- Uncertainty around our forecasts is high given unknowns about how much of President-elect Trump's campaign promises will materialize.
- Trump's policy proposals from his campaign, at face value, could result in higher inflation in the near term and lower growth in the medium to long term.

A Change In Administration Will Yield A New Regulatory Tone At The Top

- We expect leadership at several agencies to transition once the Trump administration begins its term.
- Although the supervisory approach may change, our base case is that bank regulation won't loosen significantly.
- However, the administration and new regulatory leadership may consider changes to several areas, and the timeline for implementing changes in regulation on capital, liquidity, and other requirements could be extended.

Regulatory Organization	
Federal Reserve System (Fed)	• Michael Barr will step down from his position as vice chair for supervision effective Feb. 28, 2025, allowing President Trump to nominate a replacement. • Terms of Chairman Powell and one other board member expire in 2026. • Term of Vice Chair Jefferson expires in 2027. • The three other board members have terms lasting past the next administration.
Federal Deposit Insurance Corp. (FDIC)	• President Biden nominated Christy Goldsmith Romero to replace Martin Gruenberg as chair of the five-member board at the FDIC, but the Senate has not confirmed her. • The FDIC board is made up of three presidential appointees, including the chair and vice chair, as well as the comptroller of the currency and the director of the Consumer Financial Protection Bureau. • No more than three members of the board of directors may be members of the same political party.
The Office of the Comptroller of the Currency (OCC)	• The comptroller of the currency is appointed by the treasury secretary. The appointment requires Senate confirmation. • Michael Hsu is acting comptroller but has not received Senate confirmation.
Consumer Financial Protection Bureau (CFPB)	• President can replace director
Federal Housing Finance Agency (FHFA)	• President can replace director
Securities and Exchange Commission (SEC)	• The SEC has five commissioners, appointed by the President, with staggered terms of five years. No more than three commissioners may belong to the same political party. The President also designates one of the commissioners as chair. • Chair Gary Gensler will step down on Jan. 20, 2025, allowing President Trump to nominate a replacement. • President Biden nominated one commissioner for a second term. The terms of the three other commissioners will expire during the next Presidential term.

Source: S&P Global Ratings

Many Regulatory Changes May Be Considered, But Uncertainty Remains High

- The Trump administration, Congress, and new leadership of regulatory bodies may consider changes to several parts of existing regulation, though the details, feasibility, and timelines of any plans remains very unclear.
- We will consider how any changes may support or detract from the strength and stability of the banking system and the creditworthiness of the institutions we rate.

Capital	Potential re-proposal and implementation of the final set of the Basel III capital standards. Regulators likely will consider the impact of the Basel “endgame” on the capital requirements of the global systemically-important banks (GSIBs) and other large banks. They may also re-propose the GSIB surcharge rule and determine whether and how the endgame will apply to banks with assets of $100 billion-$250 billion.
Stress Testing	The Fed will seek public comment on improving the transparency of stress tests and reducing the volatility of resulting capital buffers. This could include: • Disclosing and seeking public comment on stress test models; • Averaging results over two years; and • Ensuring the public can comment on the hypothetical scenarios used annually for the test.
Liquidity	Potential changes to the regulatory liquidity framework. The Fed previously indicated those could include: • Requiring banks of a certain size to maintain a minimum amount of readily available liquidity at the Fed's discount window, calculated relative to their uninsured deposits; • Restricting the degree to which the liquidity buffers at large banks rely on held-to-maturity securities; and • Updating the treatment of certain types of deposits in the regulatory liquidity framework.
Long-term Debt	Potential finalization of (or change to) a proposal to require any bank with at least $100 billion in assets to maintain a minimum amount of long-term debt that could be used to absorb losses in a failure. Regulators issued the proposal in August 2023 but have yet to indicate if it will be implemented as written.
Regulation	Potential effort to streamline regulation in general. Athough details on any plans from the new administration have not become clear.
CFPB Rules	Potential consideration of rules passed by the CFPB during the Biden administration, including the cap on overdraft fees.
Deposit Insurance	Potential increase in deposit insurance on business accounts.
Housing Finance Reform	Potential consideration of a prior effort to privatize and release Fannie Mae and Freddie Mac from conservatorship while reworking and limiting the government's involvement in the housing market and encouraging greater participation of private capital.

U.S. Forecast: Earnings Remain Resilient Amid Continued Economic Growth

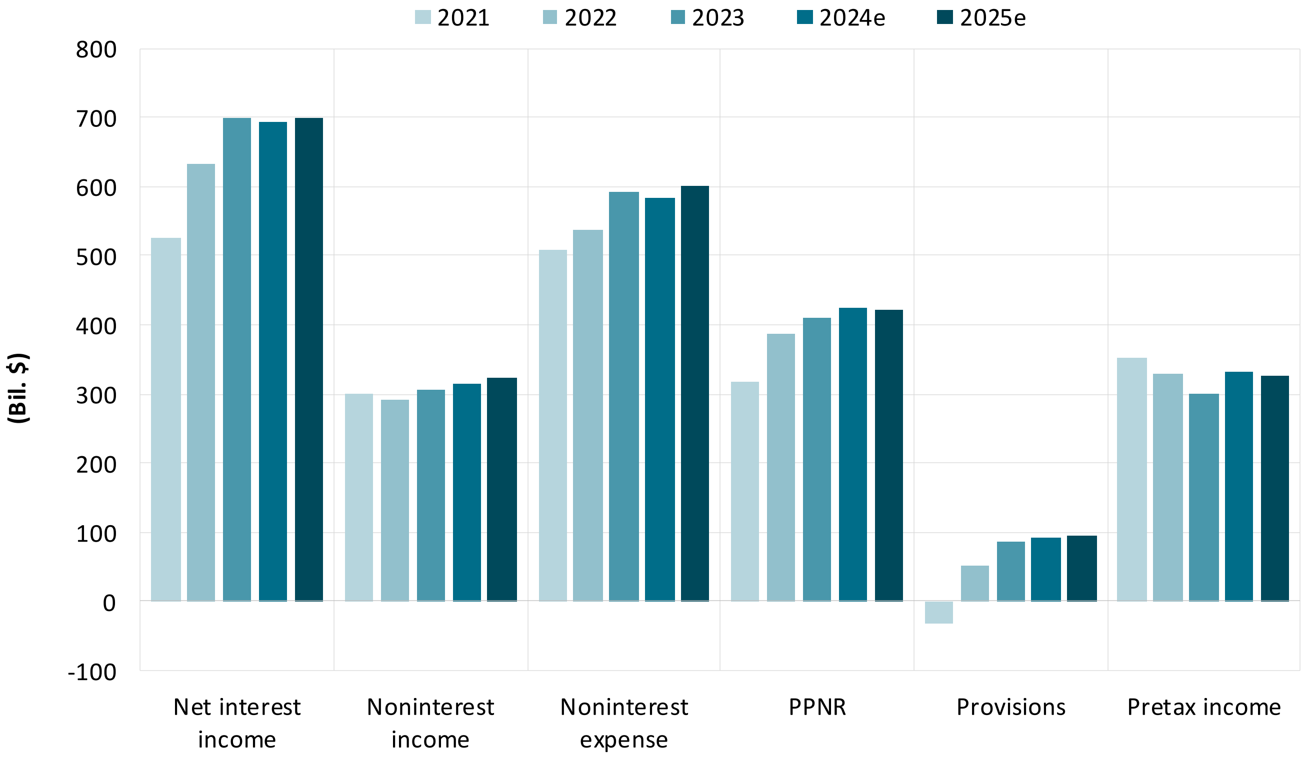
Worsening | | Neutral | | Improving

Revenues	Net interest income (NII) may grow modestly, depending on the pace of earning asset growth and the path of interest rates. Fee income may rise with lower rates supporting investment banking, wealth and asset management.
Expenses	Investments in technology, and perhaps some increase in business activity, may push expenses somewhat higher in 2025, notwithstanding banks' continued focus on cost controls.
Profitability	The banking industry should generate a return on common equity of 10.5%-11.5% in 2025, compared to an estimated 11.0%-11.5% in 2024, assuming an economic soft landing. A greater-than-expected slowdown could pull returns into the single digits.
Credit quality	Provisions and net charge-offs will likely incrementally worsen. However, an economic soft landing, if achieved, should prevent a substantial decline in asset quality.
Capital	While some banks may increase capital ratios further, many others are unlikely to boost their ratios until regulators indicate how they will implement the Basel III Endgame. Amortization and perhaps some decline in long-term rates may also lead to a drop in unrealized losses, relieving some pressure on adjusted capital ratios.
Funding and liquidity	Deposits have stabilized, and we expect limited growth in 2025, as the Fed potentially eases monetary policy. That could also support liquidity. While banks have good contingent liquidity, many still have relatively low cash balances.

Note: Forecast for next 12 months. Source: S&P Global Ratings.

Forecast | Banks Continue To Generate Relatively Good Earnings

Earnings forecast, all FDIC-insured banks



Source: S&P Global Ratings.

- In our base-case forecast, we expect banks to earn returns on common equity of about 11.0%-11.5% in 2024 and 10.5%-11.5% in 2025.
- Incremental growth of expenses and provisions may offset some rise in fee income and NII.
- We assume continued economic growth, modest loan growth, and some decline in rates while avoiding a hard landing.
- In a downside scenario, perhaps with a mild recession, higher provisions and weaker fee income would drive profitability into the single digits.

Greater-than-expected Earning Asset Growth Could Offset NIM Contraction

- While NIMs have generally fallen in past rate cutting cycles, earning asset growth has powered NII increases.
- In our base case, we forecast weaker earning asset growth in 2025 (2%-4%) than prior cycles , resulting in limited NII expansion.
- However, if banks grow earning assets at a mid-single digit rate or faster, NII likely will grow meaningfully.

(%)	Quarterly average effective fed funds rate							
Rate cycle	Start of cycle	One year into cycle	End of cycle	NIM change: One year after first decrease	NII change: One year after first decrease	NIM Change: Start to final quarter	NII CAGR: Start to final quarter	Average earning assets CAGR: Start to final quarter
Q2 2000 - Q2 2004	6.5	4.0	1.0	-0.06	3.8	-0.35	4.9	7.5
Q1 2007 - Q3 2015	5.3	2.6	0.1	-0.03	4.9	-0.28	3.7	4.8
Q1 2019 - Q4 2021	2.4	0.7	0.1	-0.25	5.2	-0.86	0.3	11.8

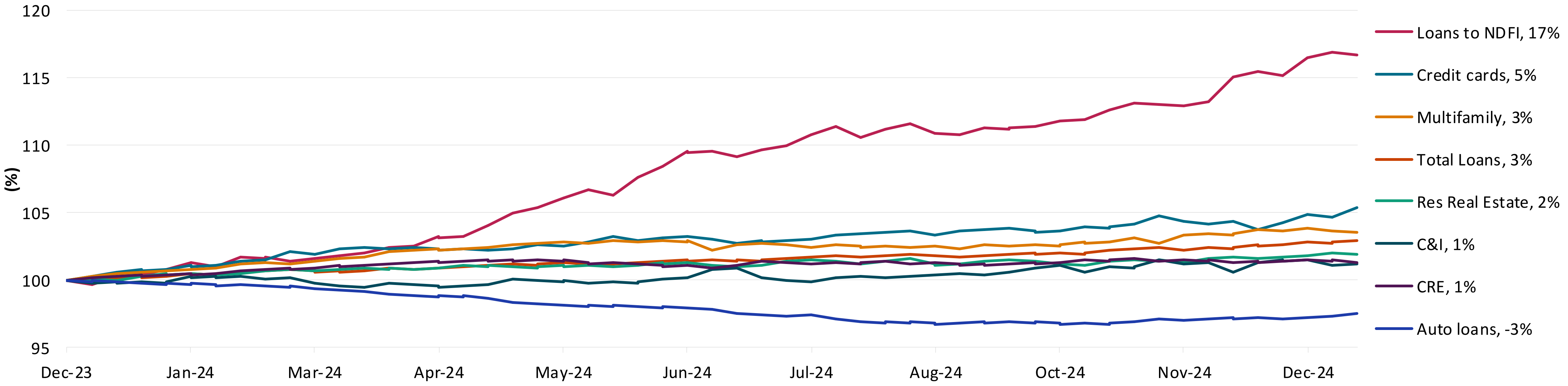
All figures are percentages. Sources: FDIC and S&P Global Ratings based on data for all FDIC-insured commercial banks.

Loan Growth May Remain Limited, Depending On The Pace Of The Economy

- Loans to nondepository financial institutions, credit cards, and multifamily loans grew fastest in 2024, while other loan categories modestly expanded.
- In our base case, we expect continued moderate overall growth. However, the pace of economic growth and the approach to regulation could affect banks' risk appetites.

One-year index of bank loan growth, all FDIC-insured banks

Dec. 2023 = 100

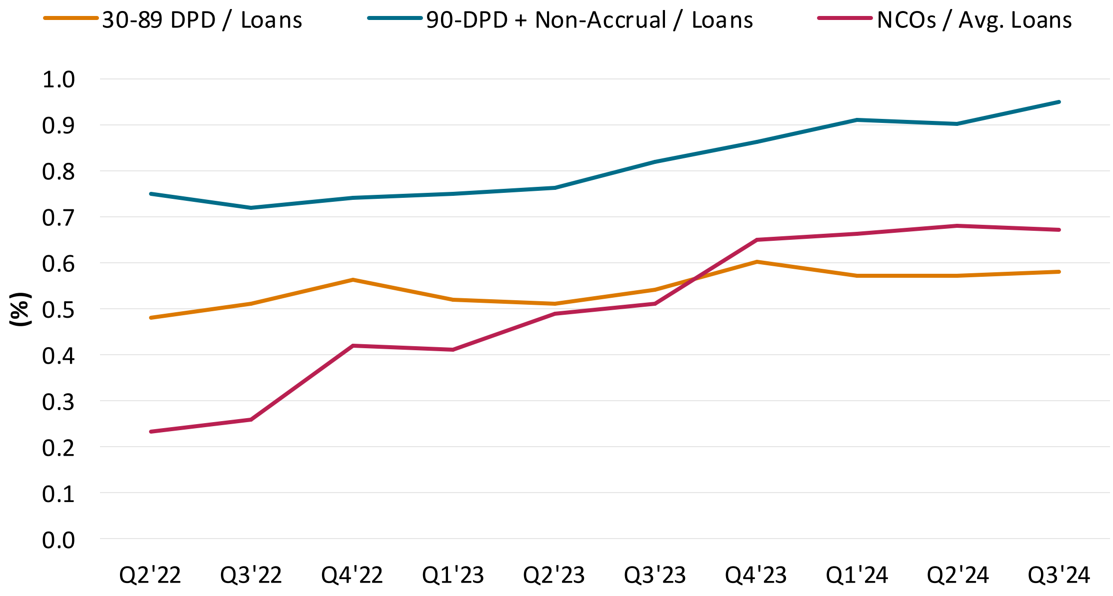


Sources: S&P Global Ratings based on Federal Reserve H.8, Assets and Liabilities of Commercial Banks in the United States.

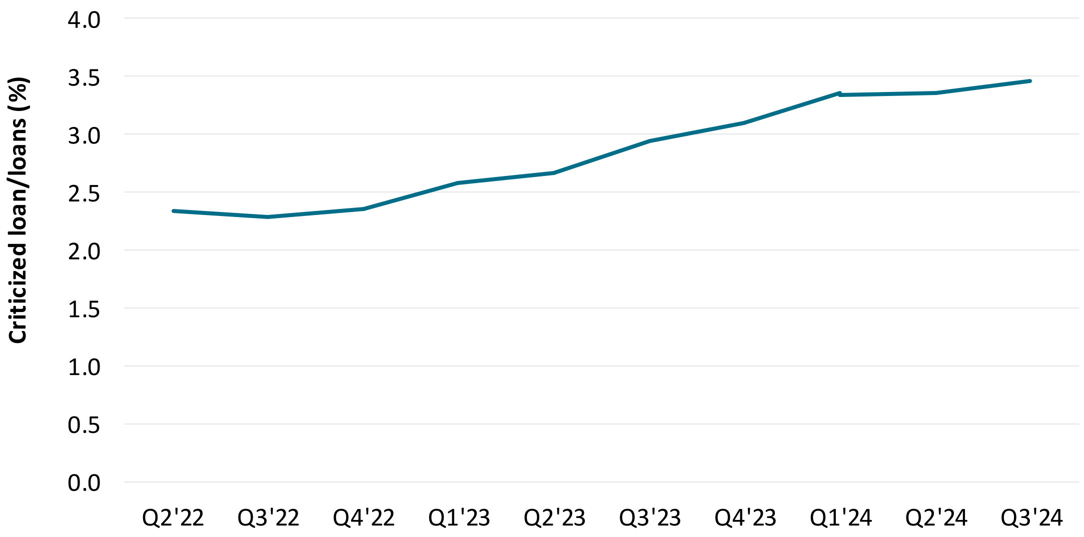
Asset Quality Will Likely Incrementally Deteriorate But Remain Manageable

- Net charge-offs, nonperforming loans, and criticized loans have increased, mostly on commercial real estate (CRE), commercial and industrial (C&I), and credit card loans.
- While we expect some further worsening in 2025, we think most rated banks are well placed to absorb deterioration without a major hit to earnings.

Asset quality metrics, all FDIC-insured banks



Criticized loans of rated banks



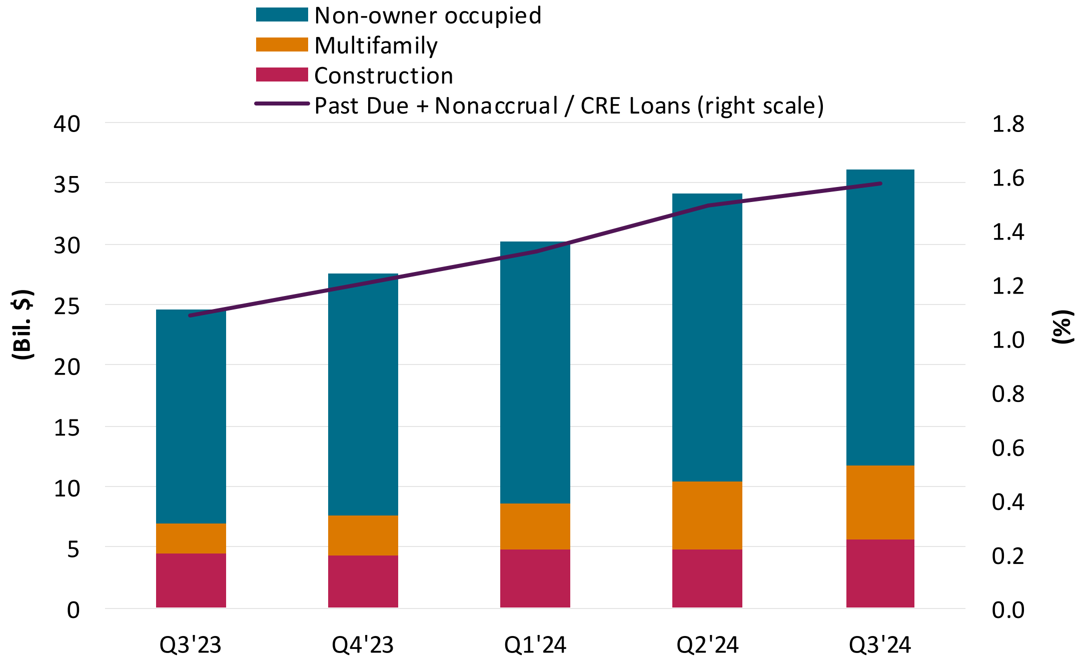
Note: DPD=days past due. All FDIC-insured banks based on aggregated call report data. Criticized loans are for 41 rated banks that have consistently reported such data for all reporting periods in the chart. Sources: S&P Global Ratings, S&P Global Market Intelligence, and regulatory filings.

S&P Global Ratings

Rated Banks Will Continue Working Through Challenges in CRE This Year

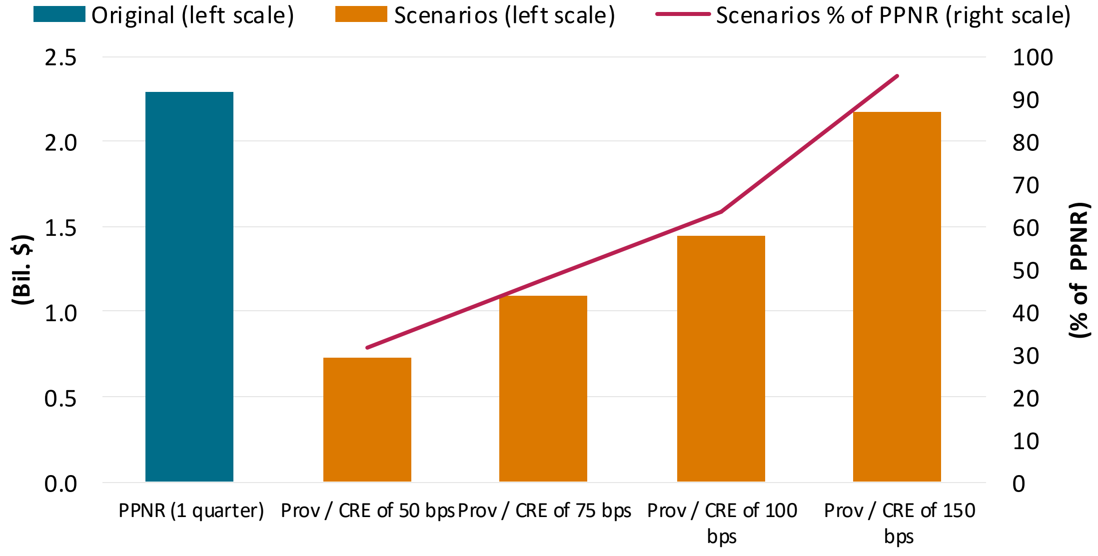
- CRE loans at least 30 days past due or on nonaccrual have gradually climbed and should increase further.
- Banks will likely take further losses as they work to resolve problem CRE loans in 2025 and 2026. In our base case, we expect rated banks to absorb such losses through allowances and earnings, but we still see some risk of greater-than-expected losses for some.

CRE past due and nonaccrual loans: all FDIC-insured banks



Sources: FDIC and S&P Global Ratings. Data as of Sep. 30, 2024

Impact of potential provisions on CRE loans to one quarter of PPNR Rated banks with CRE > 200% of Tier 1 capital, aggregated

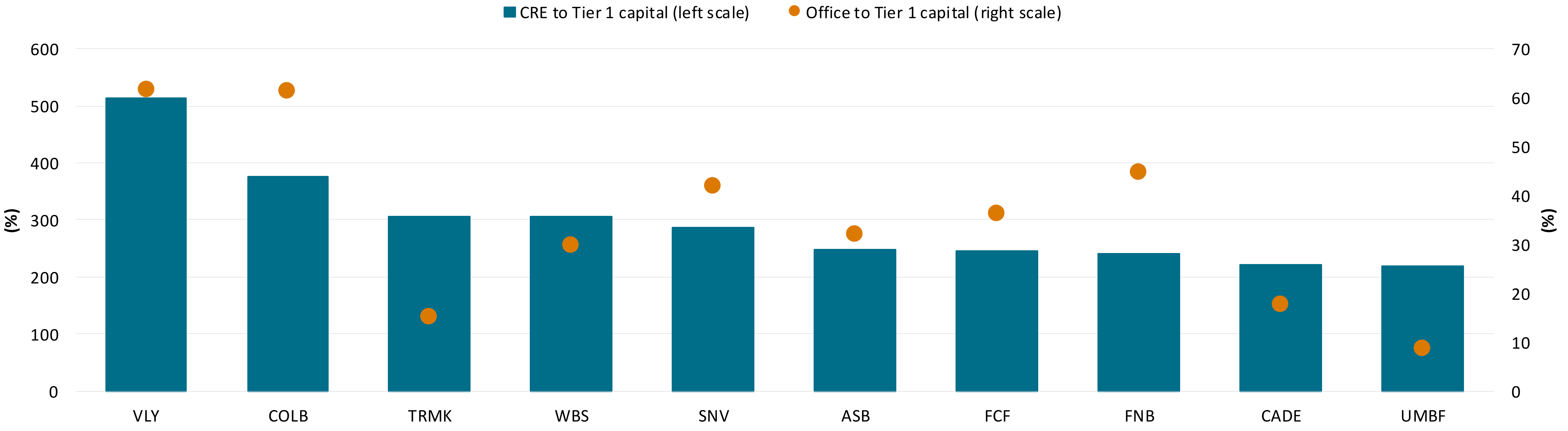


PPNR--Preprovision net revenue. bps--Basis points. Preprovision net revenue was calculated based on Q2'24 data. Source: S&P Global Ratings.

Office Loans Are A Small Portion Of Banks' CRE Portfolios, But Still Pose Risk

- Offices typically represent about 20% of total CRE loans at rated banks.
- Office exposure as a percent of Tier 1 capital ranges up to about 60% for the most exposed banks.

Office exposure for select rated banks with CRE/Tier 1 common capital above 200%

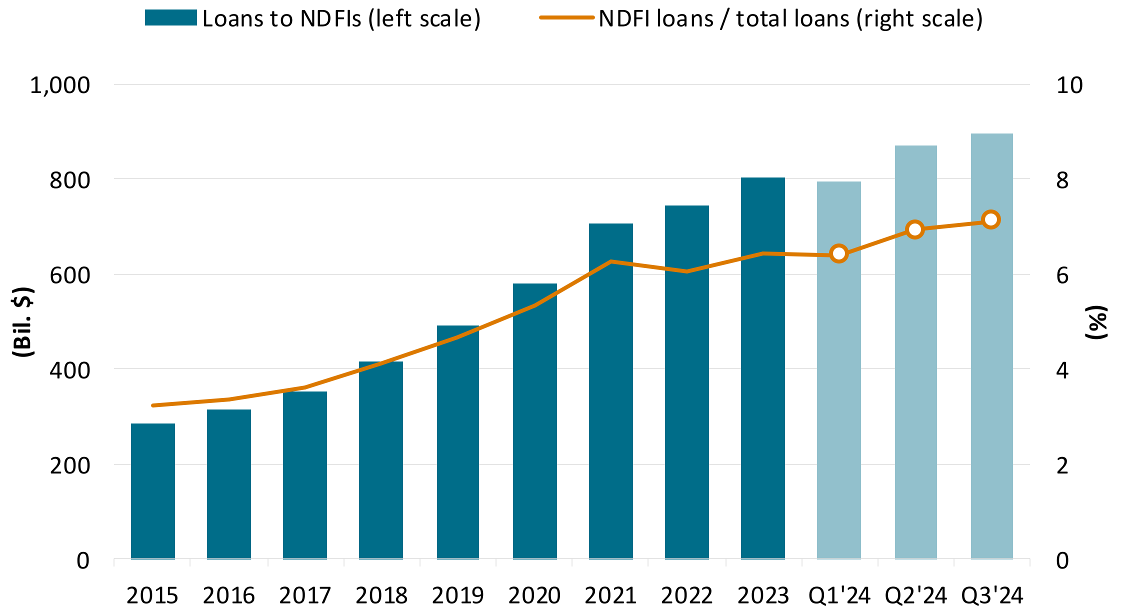


Data as of September 30, 2024. CRE--Commercial real estate. Note: Bank CRE loans exclude owner-occupied. Sources: S&P Global Ratings, FDIC, company earnings presentations, and 10-Qs.

Banks Likely Will Grow Nonbank Exposures Further, But With Protections

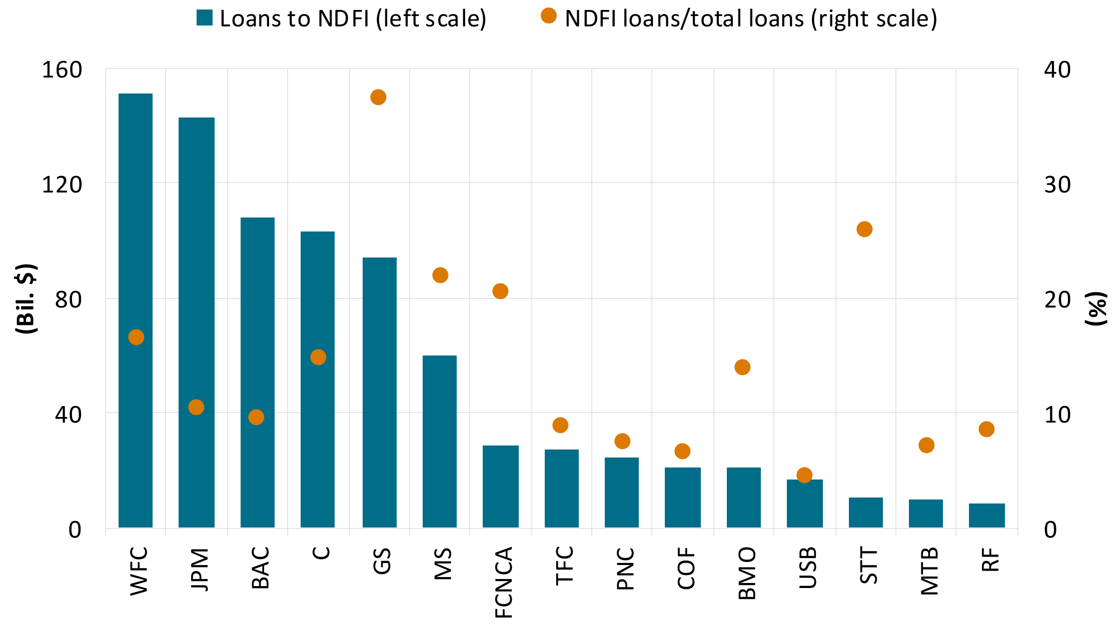
- Loans to nonbank financial institutions have risen by more than 50% since 2020 and make up about 7% of loans of FDIC-insured banks.
- This in part reflects the growth of private credit and nonbank intermediation in general.
- Collateral and good diversification by borrower type have helped mitigate risks for banks.

Loans to nondepository financial institutions



Note: All FDIC-insured banks. Source: S&P Global Ratings.

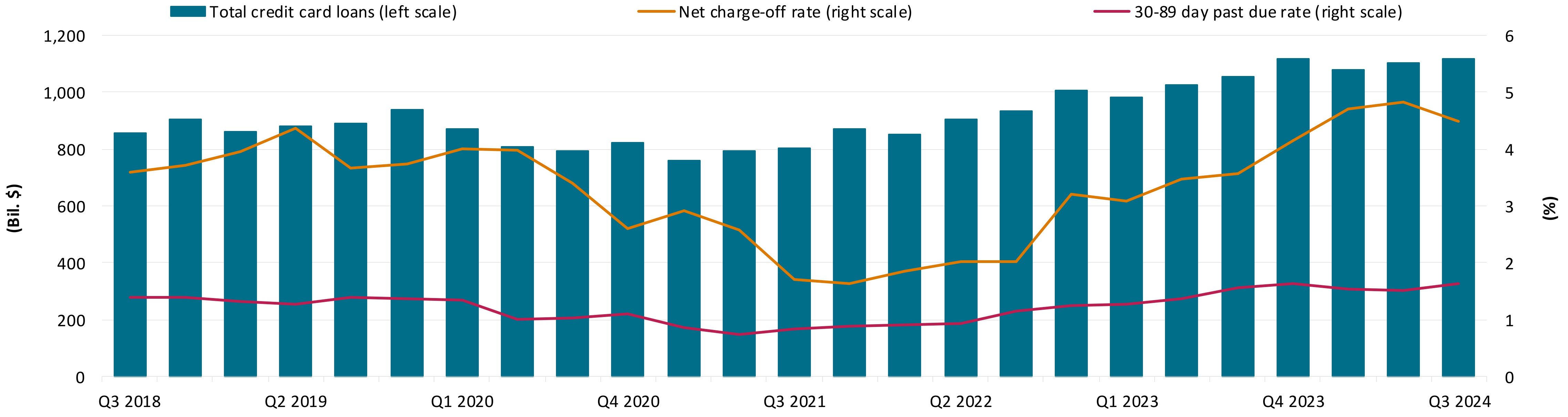
Rated banks: loans to nondepository financial institutions



Data as of September 30, 2024. Source: S&P Global Ratings.

Credit Card Loss Rates, At Multi-Year Highs, May Begin To Level Off In 2025

- With banks' card balances up about 20% in the last two years, charge-offs have risen to their highest level in more than a decade.
- However, we expect loss rates to slow or stabilize, assuming economic growth, due to the benefits of tightened underwriting.



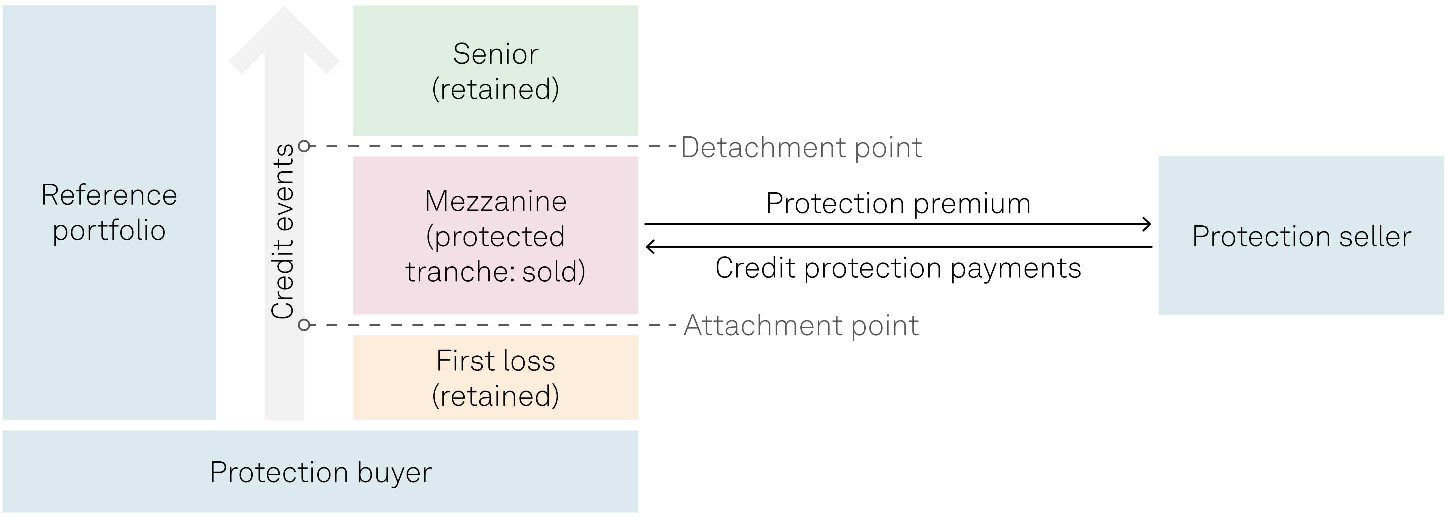
Top 10 largest credit card lenders as of third-quarter 2024 (Bil. $): sample is roughly 90% of total industry card loans

- JP Morgan: 190
- Citigroup: 170
- Capital One: 143
- American Express: 102
- Bank of America: 101
- Discover: 100
- Synchrony: 94
- Wells Fargo: 55
- Barclays US LLC: 31
- U.S. Bancorp: 29

Sources: S&P Global Ratings, FDIC Quarterly Banking Profile, and regulatory filings.

Banks May Use More SRTs For Capital And Risk Management Purposes

Credit protection agreement example



Source: S&P Global Ratings.

- U.S. banks are conducting more significant risk transfers (SRTs) through credit-linked notes (CLNs) and credit default swaps (CDS) to support their capital and to manage their risks.
- Issuance in the U.S. still trails Europe but is likely to continue increasing.
- In 2023, the Fed provided clarity pertaining to capital relief on directly issued CLNs, sparking a rise in these transactions.
- SRTs are also being conducted through special purpose entities.
- We will continue to monitor how the SRT market evolves and consider its impact on bank creditworthiness and systemic risks.

Large Banks' Capital Will Hinge On The Finalization Of The Basel III Endgame

- All category I and II banks have excess capital, but to varying degrees.
- The Basel III Endgame final rules to strengthen capital requirements will play a major role in determining capital levels for the larger banks; a lot of uncertainty remains about how and when those rules will be implemented.

Common equity Tier 1 ratio--Basel III fully phased in

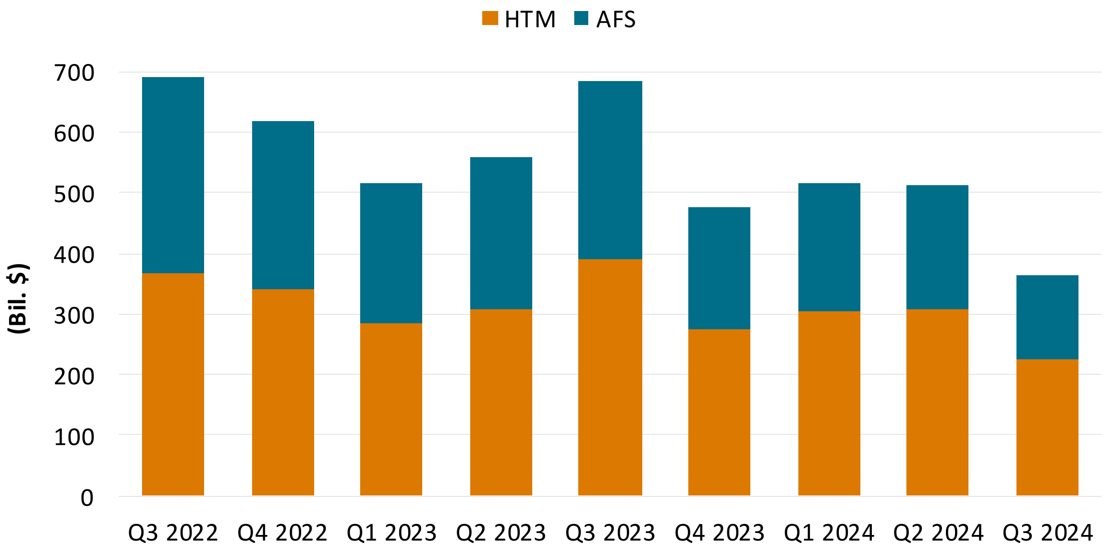
(%)	Q3 '24		Q/Q change (bps)		Stress capital buffer (SCB)	Std. CET1 minimum requirement	Current Std. CET1 surplus over minimum requirement
	Std.	Adv.	Std.	Adv.			
BAC	11.8	13.5	-10	0	3.2	10.7	1.1
C	13.7	12.2	10	0	4.1	12.1	1.6
JPM	15.3	15.5	0	0	3.3	12.3	3.0
WFC	11.3	12.7	30	40	3.8	9.8	1.5
MS	15.1	14.9	-10	-60	6.0	13.5	1.6
GS	14.6	15.5	-30	-40	6.2	13.7	0.9
BK	11.9	12.0	50	50	2.5	8.5	3.4
STT	11.6	12.5	40	50	2.5	8.0	3.6
NTRS	12.6	14.0	0	10	2.5	7.0	5.6

CET1--Common equity Tier 1 ratio.
Sources: Company filings, S&P Global Ratings, the Federal Reserve Board, and S&P Cap IQ Pro.

The Decline In Unrealized Losses On Securities Will Depend On Rates

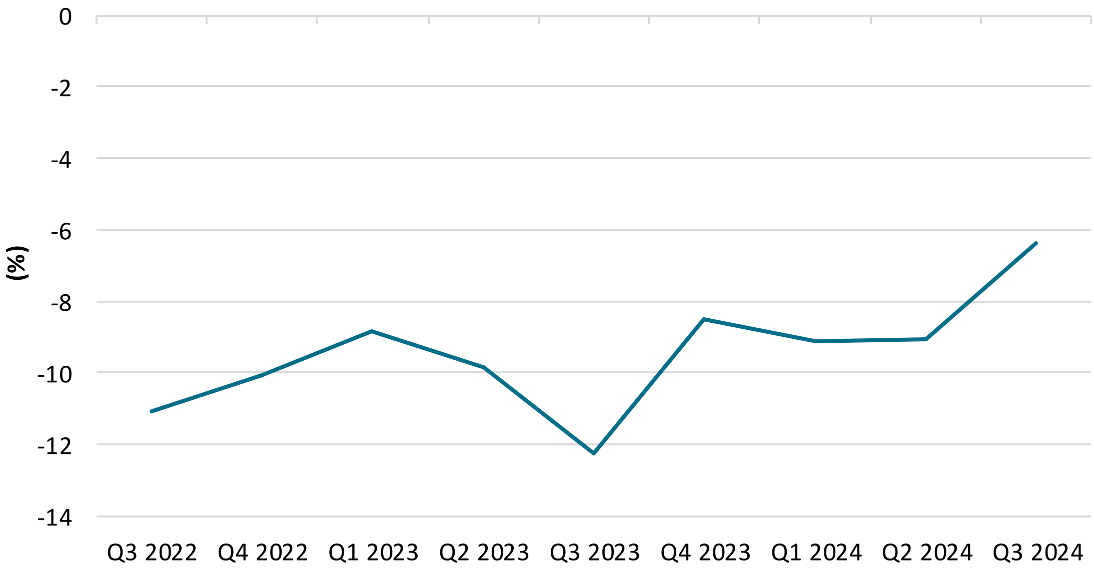
- Unrealized losses--down sharply from their peak—should decline over time as long-term securities move closer to maturity, easing some capital pressure.
- However, the path of unrealized losses will depend on long-term interest rates, which have risen in recent months. In their base case, our economists expect long-term rates to fall in 2025, though uncertainty is high.

All FDIC-insured banks: unrealized losses on securities



FDIC--Federal Deposit Insurance Corp. AFS--Available for sale. HTM--Held to maturity.
Sources: S&P Market Intelligence and FDIC.

All FDIC-insured banks: unrealized losses/total securities (HTM+AFS) / Total securities

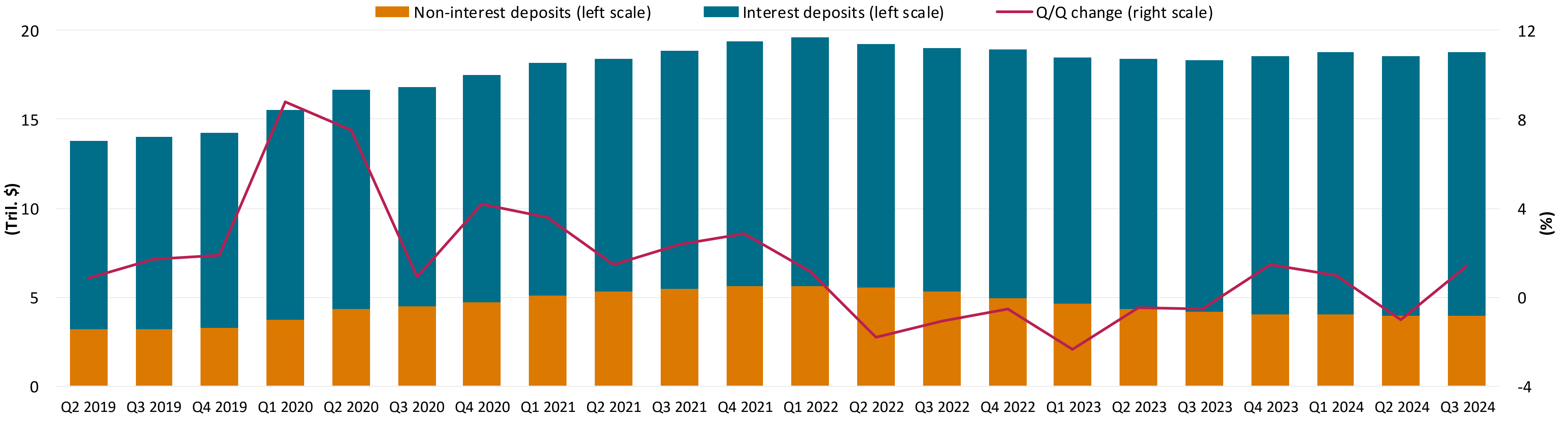


Sources: S&P Market Intelligence and FDIC.

Deposits, Up Modestly From Trough, Likely Will Improve Gradually In 2025

- A further reduction in interest rates should support deposit levels, particularly if the Fed further slows quantitative tightening.
- Non-interest bearing deposits rose sequentially in Q3 2024, the first increase since 2021.

All FDIC-insured banks: total deposits



Source: S&P Global Market Intelligence.

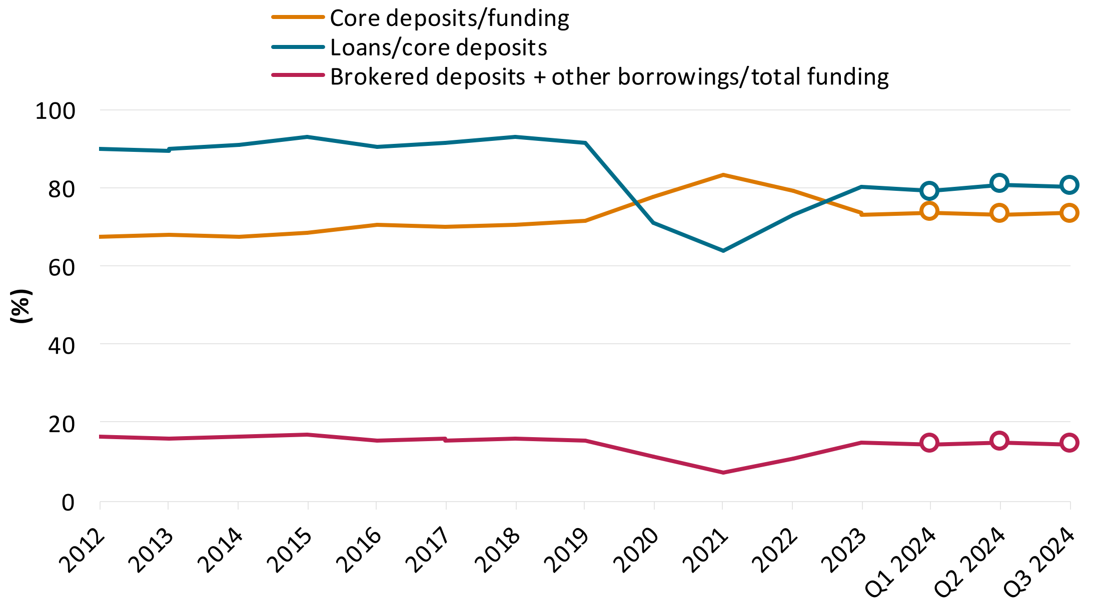
S&P Global
Ratings

Lower Rates And Deposit Growth Could Support Funding And Liquidity

- Deposit growth may help banks at least modestly bolster their funding and liquidity, but greater-than-expected loan growth could be an offset.
- Banks may also look to add to on-balance sheet liquidity following improvements they made to contingent liquidity since 2022.

Funding measures of commercial banks

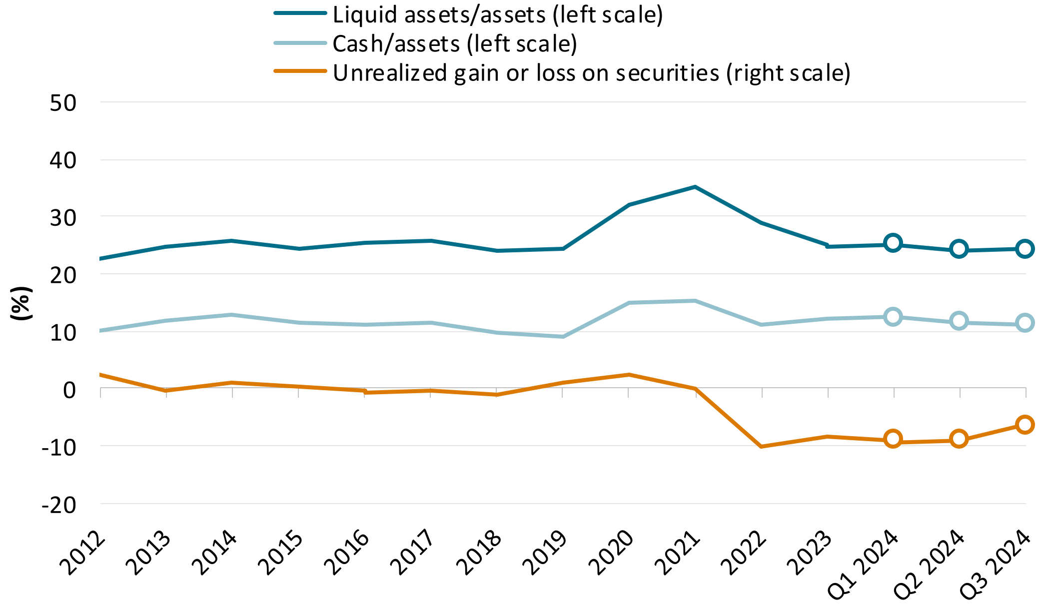
Core deposits = deposits less brokered, jumbo, and foreign deposits



Total funding includes deposits, federal funds purchased, repurchase agreements, subordinated debt, and other borrowings. Source: S&P Global Market Intelligence.

Liquidity measures of commercial banks

Liquid assets = cash + unpledged securities + Fed funds



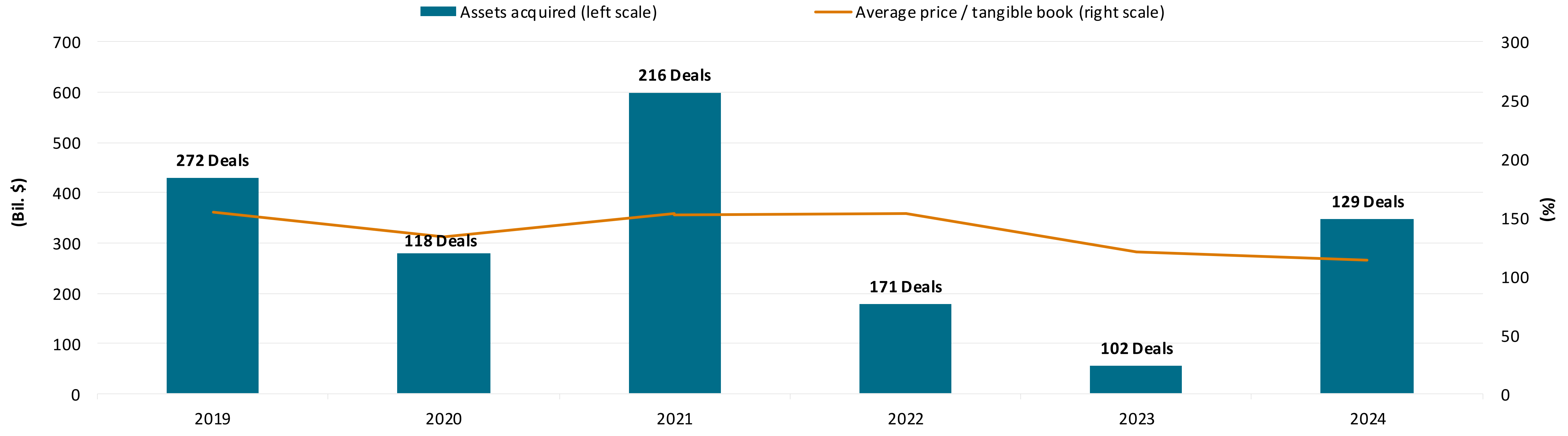
Source: S&P Global Market Intelligence.

Bank Mergers And Acquisitions Could Accelerate From A Low Level

- Financial challenges in the industry and tighter merger review standards from regulators have limited bank M&A activity.
- However, regulators, headed in part by Trump administration appointees, may be more open to approving deals. A rise in bank valuations, a decline in unrealized losses, the continuing need for scale, and pent-up demand may also spur deals.

Merger activity of U.S. banks

Based on announced date



Source: S&P Global Market Intelligence. Data as of Dec. 31, 2024. Note: Only includes deals where the target is based in the U.S. Reflects data at deal announcement event. The announcement of the acquisition of Discover Financial Services makes up a material portion of the 2024 assets acquired.

Related Research

Click to see the following research articles, or find more at www.SPRatings.com/nabanking

- Rating Component Scores For U.S., Canadian, And Bermudian Banks (December 2024), Dec. 31, 2024
- Economic Outlook U.S. Q1 2025: Steady Growth, Significant Policy Uncertainty, Nov 26, 2024
- Global Banks Outlook 2025: Cautiously Confident, Nov. 14, 2024
- How Are North American Banks Using Significant Risk Transfers?, Nov. 12, 2024
- Banking Industry Country Risk Assessment: U.S., Oct. 14, 2024
- Comparative Statistics: U.S. Banks (October 2024), Oct 9, 2024
- Your Three Minutes In U.S. Banking: What To Watch Regarding Regulation In The Upcoming Election, Sept. 9, 2024
- Tighter Liquidity Regulations Could Help Fortify The U.S. Banking Sector, Where Liquidity Risks Still Linger, July 11, 2024
- U.S. Bank Shareholder Payouts May Rise In 2024, Despite Higher Capital Depletion In Stress Test, July 3, 2024
- Outlooks On Five U.S. Regional Banks Revised To Negative From Stable On Commercial Real Estate Risks; Ratings Affirmed, Mar. 26, 2024

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