Shared National Credits Program
1st Quarter 2016 Review

Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency

Washington, D.C.

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About the Shared National Credit (SNC) Program

The SNC Program assesses credit risk and trends as well as risk management practices associated with the largest and most complex credits shared by multiple regulated financial institutions. The program provides for uniform treatment and increased efficiency in shared credit risk analysis and classification. The SNC Program is governed by an interagency agreement among the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (the agencies).

The agencies initiated a semi-annual SNC examination schedule in 2016. SNC reviews are now planned for the first and third calendar quarters with some banks receiving two examinations and the others continuing to participate in a single review each year. Results discussed in this document are based on the most recent first quarter 2016 examination concluded in April 2016 and reflect data submitted by all reporting banks.[1] Despite the increase in examination frequency, the agencies will issue a single press release annually that captures combined findings for each examination from the previous 12 months. The next press release will be published upon completion of the first quarter 2017 SNC examination.

Executive Summary

The level of adversely rated (i.e., special mention[2] and classified[3]) assets in the SNC portfolio continues to be higher than observed in previous periods of economic expansion (see Exhibit 3), leading to concern that losses could rise considerably in the next downturn. The high level of credit risk stems from a large share of risky leveraged finance loans underwritten based on weak practices, and the significant decline in oil prices since mid-2014 that has reduced the repayment capacity of obligors in the oil and gas (O&G) sector. Notwithstanding the riskiness of the existing portfolio, the agencies noted improved underwriting and risk management practices related to the most recent leveraged loan originations as underwriters continued to better align practices with regulatory expectations, and as investor risk appetite moderated away from transactions at the lower end of the credit spectrum.

I. Leveraged Lending

The first quarter 2016 SNC review found the incidence of non-pass loan originations has reduced to a de minimis level. Examiners noted continued progress toward full compliance with underwriting and risk management expectations set forth in the 2013 leveraged lending guidance[4] and subsequently issued frequently asked questions documents. However, some gaps between industry practices and the guidance remain which require continued attention by the agencies. Examiners again raised concerns about borrowers' capacity to repay certain new originations—both underwritten and refinanced loans—if economic conditions deteriorated, or if interest rates rose to historical norms. The agencies continue to be concerned that any downturn in the economy would likely result in a significant increase in the already considerable adversely rated leveraged lending exposure, especially considering the limited financial flexibility present in many of the credits not currently adversely rated. Further, some weaknesses in underwriting practices persist; examiners observed structures with ineffective or no covenants, liberal

[1] During this transition year, data reflects a period of nine months from the prior examination.

[2] See appendix A for regulatory definition of special mention.

[3] A classified commitment is an asset that is rated substandard, doubtful or loss on the regulatory scale. See appendix A.

[4] 78 Fed. Reg. 17766 (March 22, 2013).

repayment terms, incremental debt provisions,[5] that allow for increased debt which may inhibit deleveraging capacity and dilute senior secured creditor positions.

Incremental facilities continue to draw attention because of increased use, often in conjunction with relaxation of other structural elements such as covenants and restricted payments. The use of incremental facilities may also suggest that existing lenders are willing to share priority of claims with more aggressive lenders, effectively outsourcing a bank's risk appetite and diminishing internal underwriting controls. As was observed in 2015, this SNC examination noted instances where incremental facilities have been used for dividends and other purposes that weaken a borrower's underlying credit fundamentals and coincided with softened constraints that would limit lender remedies if needed.

II. Oil and Gas Lending

The severe and prolonged decline in energy prices since 2014 has caused financial stress to many energy companies, particularly non-investment grade and unrated exploration and production (E&P) and energy service companies. Increasing credit risk from reduced revenue has been exacerbated by the high leverage of some E&P companies, primarily resulting from debt-funded acquisitions during the recent drilling expansion activity, and corresponding reductions in liquidity. The low commodity price environment and declining hedging programs of many companies have caused critical reductions in operating cash flow and lower valuations of reserve assets used to secure financing for further development. Many energy companies have responded by taking actions to reduce operating costs and overhead, while preserving liquidity through asset sales, issuance of additional debt and equity instruments, and drawing on remaining senior bank commitments.

Generally, banks have shown flexibility in working with borrowers by relaxing financial covenants to allow borrowers time to develop strategies to curtail borrowing base over-advances, reduce leverage, and reestablish profitable operations. Nonetheless, the reductions in liquidity and unsustainable debt burdens from excessive accumulation of second lien and unsecured debt have resulted in a dramatic increase in borrower defaults and bankruptcy filings, which is expected to continue through 2016. Bank commitments to these borrowers are primarily in a senior secured position with the lowest risk of loss.

III. SNC Portfolio: Volume, Credit Quality and Trends

Overall SNC Portfolio

The 2016 SNC portfolio totaled $4.1 trillion, with 10,837 credit facilities to 6,676 borrowers (see Exhibit 1). Appendix C contains a breakout of SNC results by major industry groups.[6]

[5] Based on SNC examination data, 90.6 percent of leveraged loans originated after June 1, 2015 contained incremental debt provisions that allow obligors to incur additional debt under the existing loan documentation, most often without existing lender consent.

[6] The agencies introduced industry data in 2008 that presented industries vertically along product origination and distribution lines. The review places credits in seven primary sectors, largely following the outline of the 2007 U.S. Census Bureau North American Industry Classification System (NAICS) codes (see appendix C).

Exhibit 1: Overall Credit Facilities and Commitment Trends

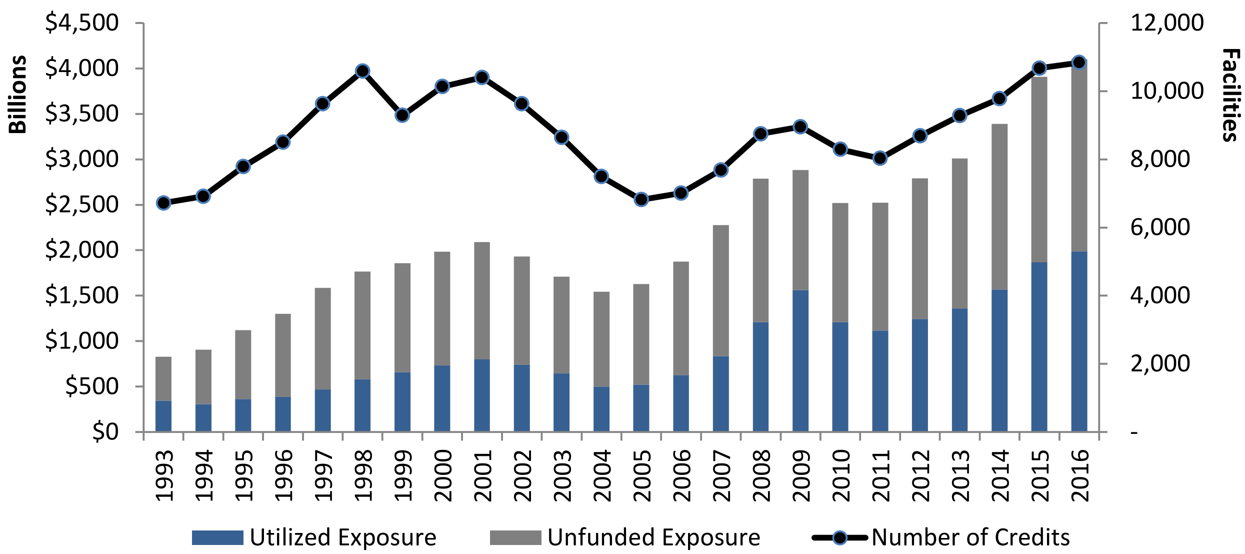


Exhibit 2 below details the year-over-year trends in overall SNC commitment amounts.

Exhibit 2: Trends in Overall SNC Special Mention, Classifieds and Nonaccrual Commitments

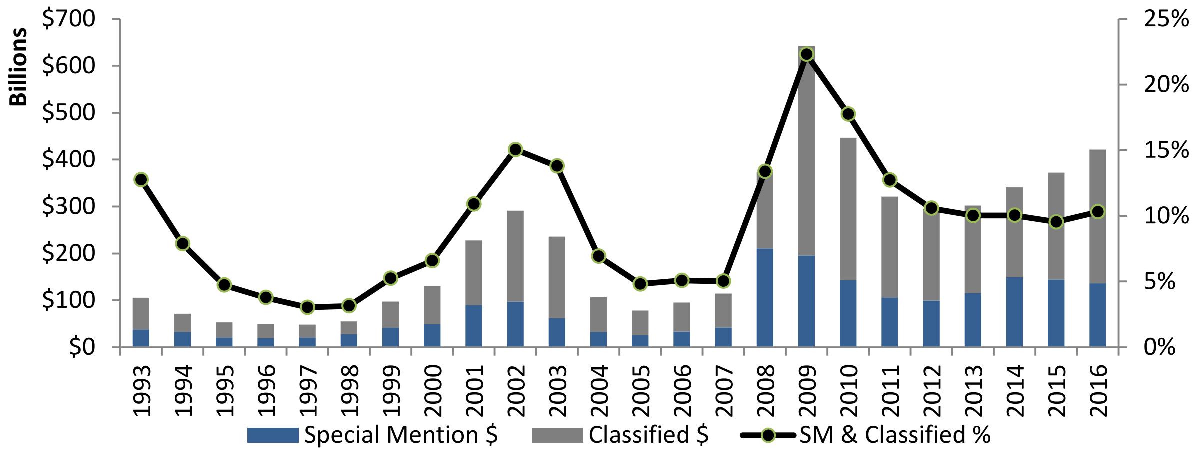
	2015 Commitments ($ Billion)	1Q16 Commitments ($ Billion)	1Q16 vs. 2015 ($ Billion)	1Q16 vs. 2015 (%)
SNC Portfolio Commitments	$3,908.8	$4,102.3	$193.5	5.0%
SNC Portfolio Outstanding	$1,867.1	$1,986.5	$119.4	6.4%
SNC Portfolio Borrowers	6,571	6,676	105	1.6%
SM and Classified Commitments	$372.6	$421.4	$48.8	13.0%
SM Commitments	$144.2	$136.4	($7.8)	-5.4%
Classified Commitments	$228.4	$285.1	$56.7	24.8%
Nonaccrual Commitments	$51.3	$72.6	$21.4	41.7%

Note: Nonaccrual amounts are net of loss dispositions.

The percentages of non-pass and classified commitments increased to 10.3 percent and 6.9 percent compared with 9.5 percent and 5.8 percent in 2015, respectively.[7]

[7] The non-pass credits and related ratios do not include the effects of hedging or other techniques that organizations may use to mitigate risk.

Exhibit 3: Overall Special Mention and Classified Volume and Percentage Trends



Rather than using a period of low rates to de-lever their balance sheets as has been typical in past cycles, borrowers have taken on additional debt, which may be more difficult to service in the years ahead. The special mention and classified asset ratio continues to be double that of the pre-crisis period. The agencies remain concerned about the overall level of special mention and classified commitments, as they have not recovered to the same level as previous periods of economic expansion in the mid-1990s and in the 2003-2007 period (see Exhibit 3).

Leveraged Lending

The first quarter 2016 SNC review included an examination of 24.5 percent of leveraged SNC borrowers, representing 37.0 percent of all leveraged loans by dollar commitment (see Exhibit 4).

Exhibit 4: SNC Leveraged Lending Exposure and Review Sample

	2015 SNC Examination ($ billion)	1Q16 SNC Examination ($ billion)	1Q16 vs. 2015
SNC Leveraged Lending Commitments	$957.7	$971.2	$13.4
Sampled SNC Leveraged Lending Commitments	$597.8	$359.2	($238.6)
SNC Leveraged Lending Obligors	1,395	1,399	4
Sampled SNC Leveraged Lending Obligors	610	343	(267)

Note: Sampled data comparison between 1Q16 and 2015 SNC examinations should be in context of semi-annual examinations in 2016 and beyond.

Leveraged lending is the primary contributor to the overall SNC special mention and classified rate of 10.3 percent. Leveraged loans make up 72.6 percent of all SNC special mention commitments, 58.6 percent of all substandard loans, 66.2 percent of all doubtful loans, and 56.5 percent of all nonaccrual loans.

Oil and Gas Lending

The first quarter 2016 O&G SNC portfolio represents 12.3 percent of the total $4.1 trillion in reported SNCs. The first quarter 2016 SNC review included an examination of 20.7 percent of O&G SNC borrowers, representing 24.9 percent of all O&G loans by dollar commitment.

Exhibit 5: SNC Oil and Gas Lending Exposure and Review Sample

	2015 SNC Examination ($ billion)	1Q16 SNC Examination ($ billion)	1Q16 vs. 2015
SNC O&G Lending Commitments	$480.2	$502.9	$22.8
Sampled SNC O&G Lending Commitments	$137.0	$125.4	($11.6)
SNC O&G Lending Obligors	720	735	15
Sampled SNC O&G Lending Obligors	211	152	(59)

Note: 2015 O&G commitments have been updated (revised) to reflect the inclusion of expanded industry NAICS codes.

SNC examination data showed classified O&G borrowers totaled $77.0 billion or 27.0 percent of total classified commitments in first quarter 2016, compared with $38.2 billion or 16.7 percent in 2015.

IV. SNC Portfolio: Ownership of Risk

U.S. banks continue to be the largest holders of SNC commitments, followed by foreign bank organizations (FBOs) and non-bank entities.

Exhibit 6: Distribution of SNC Commitments by Lender Type

Lender Type	2015 Total Commitments ($ billion)	1Q16 Total Commitments ($ billion)	2015 % Total Commitments	1Q16 % Total Commitments
U.S. Banks	$1,692.4	$1,840.4	43.3%	44.9%
FBOs	$1,316.6	$1,377.3	33.7%	33.6%
Non-Banks	$899.8	$884.7	23.0%	21.6%
Total	$3,908.8	$4,102.3	100.0%	100.0%

Note: Non-banks include securitization pools, hedge funds, insurance companies, and pension funds.

Non-bank entities continued to be the primary buyers of riskier loans, as they hold a disproportionate share of classified commitments (see Exhibit 7) compared with their overall ownership of the SNC portfolio (see Exhibit 6).

Exhibit 7: Distribution of SNC Special Mention and Classified Commitments by Lender Type

Lender Type	1Q16 Special Mention and Classified ($ billion)	1Q16 Special Mention and Classified (% Share Held by Lender Type)	1Q16 Special Mention and Classified (% Share of Total Commitments)
U.S. Banks	$93.8	22.3%	2.3%
FBOs	$71.5	17.0%	1.7%
Non-Banks	$256.2	60.8%	6.2%
Total	$421.4	100.0%	10.3%

Note: Non-banks also owned $41.8 billion or 57.5 percent of all nonaccrual loans.

Additional detail on supervisory definitions, outstanding balances, industry trends, exposure by entity type and loan maturity can be found in the Appendix section of this document.

Appendix A: Definitions

- **Credit Facilities**: Credit facilities include syndicated loans and loan commitments, letters of credit, and commercial leases, and other forms of credit. Commitment amounts include both drawn and undrawn portions of the loans, or facilities. The SNC review reports only the par amounts of commitments, which may differ from the amounts at which loans are carried by investors.
- **Doubtful**: Doubtful commitments have all the weaknesses of commitments classified substandard and when the weaknesses make collection or liquidation in full, on the basis of available current information, highly questionable or improbable.
- **Loss**: Commitments classified as loss are uncollectible and of so little value that their continuance as bankable commitments is not warranted. Amounts classified as loss should be promptly charged off. This classification does not mean that there is no recovery or salvage value, but rather that it is not practical or desirable to defer writing off these commitments, even though some value may be recovered in the future.
- **Nonaccrual**: Nonaccrual loans are defined for regulatory reporting purposes as loans and lease financing receivables that are required to be reported on a nonaccrual basis because (a) they are maintained on a cash basis owing to a deterioration in the financial position of the borrower, (b) payment in full of interest or principal is not expected, or (c) principal or interest has been in default for 90 days or longer, unless the obligation is both well secured and in the process of collection.
- **Non-pass Loan:** A non-pass loan is any loan that is rated special mention, substandard, or doubtful.
- **Pass**: A credit that is in good standing and is not criticized in any way.
- **Shared National Credit (SNC)**: A shared national credit is any loan or formal loan commitment, and any asset such as real estate, stocks, notes, bonds, and debentures taken as debts previously contracted, extended to borrowers by a federally supervised institution, its subsidiaries, and affiliates, that aggregates to $20 million or more and is shared by three or more unaffiliated federally supervised institutions, or a portion of which is sold to two or more unaffiliated federally supervised institutions. The threshold of $20 million has remained unchanged since the first report in 1977.
- **Special Mention**: Special mention commitments have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses could result in further deterioration of the repayment prospects, or in the institutions' credit position in the future. Special mention commitments are not adversely rated and do not expose institutions to sufficient risk to warrant adverse rating.
- **Special Mention and Classified Commitments**: This includes all commitments rated special mention, substandard, doubtful, and loss. Classified commitments include commitments rated substandard, doubtful, and loss. The agencies' uniform loan classification standards and examination manuals define these risk rating classifications. Loans that are special mention and classified are considered non-pass loans.
- **Substandard**: Substandard commitments are inadequately protected by the current sound worth and paying capacity of the obligor, or of the collateral pledged, if any. Substandard commitments have well-defined weaknesses that jeopardize the liquidation of the debt and present the distinct possibility that the institution will sustain some loss if deficiencies are not corrected.

Appendix B

Committed and Outstanding Balances (Dollars in Billions)								
Year	**Special Mention**	**Sub-Standard**	**Doubtful**	**Loss**	**Total Classified**	**Total SM and Classified**	**Total Committed**	**Total Outstanding**
1989	24.0	18.5	3.5	0.9	22.9	46.9	692	245
1990	43.1	50.8	5.8	1.8	58.4	101.5	769	321
1991	49.2	65.5	10.8	3.5	79.8	129.0	806	361
1992	50.4	56.4	12.8	3.3	72.5	122.9	798	357
1993	31.7	50.4	6.7	3.5	60.6	92.3	806	332
1994	31.4	31.1	2.7	2.3	36.1	67.5	893	298
1995	18.8	25.0	1.7	1.5	28.2	47.0	1,063	343
1996	16.8	23.1	2.6	1.4	27.1	43.9	1,200	372
1997	19.6	19.4	1.9	0.9	22.2	41.8	1,435	423
1998	22.7	17.6	3.5	0.9	22.0	44.7	1,759	562
1999	30.8	31.0	4.9	1.5	37.4	68.2	1,829	628
2000	36.0	47.9	10.7	4.7	63.3	99.3	1,951	705
2001	75.4	87.0	22.5	8.0	117.5	192.8	2,049	769
2002	79.0	112.0	26.1	19.1	157.1	236.1	1,871	692
2003	55.2	112.1	29.3	10.7	152.2	207.4	1,644	600
2004	32.8	55.1	12.5	6.4	74.0	106.8	1,545	500
2005	25.9	44.2	5.6	2.7	52.5	78.3	1,627	522
2006	33.4	58.1	2.5	1.2	61.8	95.2	1,874	626
2007	42.5	69.6	1.2	0.8	71.6	114.1	2,275	835
2008	210.4	154.9	5.5	2.6	163.1	373.4	2,789	1,208
2009	195.3	337.1	56.4	53.3	446.8	642.1	2,881	1,563
2010	142.7	256.4	32.6	15.4	304.5	447.2	2,519	1,210
2011	106.4	190.7	14.0	9.9	214.6	321.0	2,524	1,118
2012	99.3	161.7	29.5	4.6	195.8	295.1	2,792	1,243
2013	115.0	164.5	14.5	8.0	187.0	302.0	3,011	1,362
2014	149.2	171.0	11.8	7.8	191.3	340.6	3,389	1,568
2015	144.2	203.2	20.6	4.6	228.4	372.6	3,909	1,867
2016	136.4	250.7	25.7	8.6	285.1	421.4	4,102	1,986

Note: Figures may not add to totals due to rounding

Appendix C

Summary of Shared National Credit Industry Trends

(Dollars in Billions)

Industry	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Services											
Commitment	464.0	589.3	779.0	820.1	735.4	701.3	784.9	821.2	927.3	1,062.1	1,101.5
Classified	20.1	18.1	45.0	156.5	120.1	92.3	92.8	86.2	85.5	74.9	90.8
Special Mention	13.3	14.3	106.6	81.5	73.1	57.3	43.2	47.3	65.2	68.1	54.2
% Classified	4.3%	3.1%	5.8%	19.1%	16.3%	13.2%	11.8%	10.5%	9.2%	7.1%	8.2%
% Special Mention	2.9%	2.4%	13.7%	9.9%	9.9%	8.2%	5.5%	5.8%	7.0%	6.4%	4.9%
Commodities											
Commitment	364.1	439.6	578.1	658.8	592.3	593.0	665.0	709.5	788.6	904.5	937.9
Classified	18.3	10.7	12.7	77.8	57.7	42.5	34.8	39.4	43.5	72.1	114.6
Special Mention	7.6	7.0	53.6	34.9	20.4	14.0	22.4	27.7	30.0	23.1	35.7
% Classified	5.0%	2.4%	2.2%	11.8%	9.7%	7.2%	5.2%	5.6%	5.5%	8.0%	12.2%
% Special Mention	2.1%	1.6%	9.3%	5.3%	3.4%	2.4%	3.4%	3.9%	3.8%	2.5%	3.8%
Financial											
Commitment	431.1	506.3	541.0	470.9	391.3	435.4	462.6	521.9	598.3	691.7	752.0
Classified	2.1	19.2	32.5	60.4	32.6	27.6	24.7	25.3	26.7	32.2	24.7
Special Mention	2.9	3.3	13.7	28.0	17.7	9.6	9.6	12.1	19.6	20.5	18.4
% Classified	0.5%	3.8%	6.0%	12.8%	8.3%	6.3%	5.3%	4.8%	4.5%	4.6%	3.3%
% Special Mention	0.7%	0.7%	2.5%	5.9%	4.5%	2.2%	2.1%	2.3%	3.3%	3.0%	2.4%
Manufacturers											
Commitment	289.4	339.4	405.0	436.6	368.4	385.2	431.4	480.1	531.8	599.2	632.8
Classified	18.8	18.8	39.8	78.4	27.2	17.0	16.6	15.7	16.5	23.3	30.5
Special Mention	8.1	10.8	13.2	16.3	7.6	4.3	7.7	13.0	16.6	21.3	13.6
% Classified	6.5%	5.5%	9.8%	18.0%	7.4%	4.4%	3.9%	3.3%	3.1%	3.9%	4.8%
% Special Mention	2.8%	3.2%	3.3%	3.7%	2.1%	1.1%	1.8%	2.7%	3.1%	3.6%	2.1%
Real Estate											
Commitment	159.2	203.6	241.6	244.4	198.2	164.8	164.8	171.9	222.1	262.3	284.9
Classified	0.6	2.9	25.3	49.2	45.9	23.7	14.4	5.1	3.9	5.8	6.6
Special Mention	0.5	2.2	9.2	22.3	15.3	11.4	6.9	2.1	2.0	2.3	3.6
% Classified	0.4%	1.4%	10.5%	20.1%	23.1%	14.4%	8.8%	3.0%	1.7%	2.2%	2.3%
% Special Mention	0.3%	1.1%	3.8%	9.1%	7.7%	6.9%	4.2%	1.2%	0.9%	0.9%	1.3%
Distribution											
Commitment	146.1	175.7	216.0	220.5	199.0	225.9	268.7	291.3	306.5	369.8	373.4
Classified	1.5	1.9	7.7	23.2	19.6	10.0	10.7	11.8	11.0	16.7	15.0
Special Mention	0.9	4.7	13.9	12.1	8.4	9.8	8.9	12.4	15.9	8.5	11.0
% Classified	1.0%	1.1%	3.6%	10.5%	9.9%	4.4%	4.0%	4.1%	3.6%	4.5%	4.0%
% Special Mention	0.6%	2.7%	6.4%	5.5%	4.2%	4.4%	3.3%	4.3%	5.2%	2.3%	2.9%
Government											
Commitment	20.1	21.6	28.6	29.9	34.0	18.5	14.6	15.3	15.8	19.1	19.8
Classified	0.4	0.1	0.0	1.2	1.5	1.5	1.6	3.4	4.2	3.5	2.9
Special Mention	0.1	0.1	0.1	0.2	0.1	0.0	0.5	0.3	0.2	0.4	0.0
% Classified	1.8%	0.5%	0.0%	4.0%	4.3%	8.4%	11.0%	22.4%	26.7%	18.2%	14.6%
% Special Mention	0.4%	0.2%	0.4%	0.7%	0.4%	0.0%	3.4%	2.1%	1.4%	2.1%	0.0%
All Industries (Total)											
Commitment	1,873.9	2,275.4	2,789.2	2,881.2	2,518.5	2,524.2	2,792.0	3,011.1	3,390.5	3,908.8	4,102.3
Classified	61.8	71.7	163.1	446.8	304.5	214.6	195.8	187.0	191.3	228.4	285.1
Special Mention	33.4	42.4	210.4	195.3	142.7	106.4	99.3	115.0	149.4	144.2	136.4
% Classified	3.3%	3.2%	5.8%	15.5%	12.1%	8.5%	7.0%	6.2%	5.6%	5.8%	6.9%
% Special Mention	1.8%	1.9%	7.5%	6.8%	5.7%	4.2%	3.6%	3.8%	4.4%	3.7%	3.3%

Appendix D: Exposure by Entity Type

Share of Total Commitments (%)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
US Banking Institutions	44.3	42.7	41.1	40.8	40.8	41.5	43.2	44.4	43.4	43.3	44.9
FBOs	41.5	41.4	39.0	38.0	37.9	38.3	36.9	35.8	34.5	33.7	33.6
Nonbanks	14.3	15.9	19.9	21.2	21.3	20.2	19.8	19.7	22.1	23.0	21.6

Total Classifications ($ billion)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
US Banking Institutions	13.1	19.2	47.2	134.8	81.6	49.4	35.8	29.2	25.6	40.7	63.9
FBOs	17.3	17.6	45.9	101.8	62.0	41.7	37.8	32.4	25.1	34.8	54.0
Nonbanks	31.5	34.8	70.0	210.2	160.9	123.5	122.2	125.4	140.6	153.0	167.2
Totals	61.8	71.6	163.1	446.8	304.5	214.6	195.8	187.0	191.3	228.4	285.1

Classifieds as % of Commitments

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
US Banking Institutions	1.6	2.0	4.1	11.5	7.9	4.7	3.0	2.2	1.7	2.4	3.5
FBOs	2.2	1.9	4.2	9.3	6.0	4.3	3.7	3.0	2.1	2.6	3.9
Nonbanks	11.8	9.6	12.6	34.4	30.0	24.3	22.1	21.1	18.8	17.0	18.9
Totals	3.3	3.1	5.8	15.5	12.1	8.5	7.0	6.2	5.6	5.8	6.9

Total Nonaccrual Commitments ($ billion)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
US Banking Institutions	2.8	0.8	7.4	46.8	35.6	22.0	12.9	7.9	5.4	7.6	15.0
FBOs	4.7	0.9	5.6	35.5	28.6	18.1	15.9	11.2	6.5	7.2	15.9
Nonbanks	10.2	2.2	9.3	89.8	87.0	61.0	56.9	49.7	39.2	39.7	41.8
Totals	17.7	3.9	22.3	172.1	151.2	101.1	85.6	68.8	51.1	54.5	72.6

Note: Figures may not add to totals due to rounding

Appendix E: Maturity Profile