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Banks just sent this upbeat signal about the economy. Here's why investors aren't buying it.

Most banks set aside less money to cover troubled loans last quarter, despite some of Wall Street's biggest names raising alarm bells about loan quality

By [Steve Gelsi](#) and [Philip van Doorn](#)

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Banks put away money every quarter for bad loans in the form of provisions for credit losses. Photo: Getty Images/iStockphoto

Banks stockpiled less money for troubled loans during the most recent quarter despite fears over bad-debt “cockroaches.”

That’s the case even though regional-bank stocks haven’t recovered from a beating taken during third-quarter earnings season related to investors’ concerns about loan quality.

Quarterly provisions for credit losses from the 100 largest publicly traded U.S. banks were down in the third quarter from the previous quarter as well as from the year-ago period, according to data provided by LSEG and compiled by MarketWatch.

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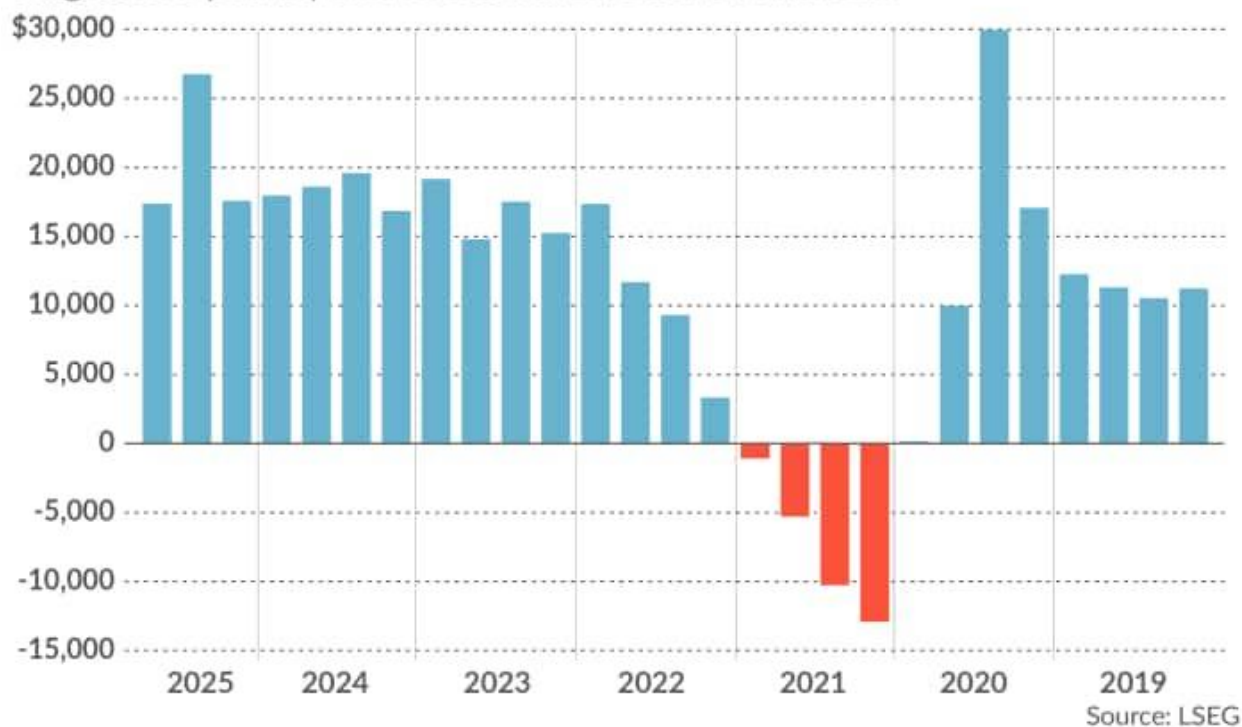
Banks set aside less money to cover troubled loans, despite some of Wall Street’s biggest names raising alarm bells about loan quality following the collapse of a major player in the subprime auto-loan industry and another in the car-parts business.

This may leave banks more vulnerable to unexpected shocks, even as they devote larger parts of their lending to more opaque forms of credit such as loans to non-depository financial institutions.

If there are more major bankruptcies ahead, big loan losses could restrict the flow of capital into the economy and hurt GDP growth should banks need to reverse course and quickly build up their loan-loss reserves.

Quarterly provisions for loan loss reserves

Largest 100 publicly traded U.S. banks. Data is in millions.



Loan-loss provisions at the 100 largest U.S. banks declined during the third quarter from both the previous quarter and the year-earlier level. Banks' provisions for loan losses were negative during 2021. As a group, they released loan-loss reserves that year, as the rate of loan losses turned out to be lower than they had expected. Photo: LSEG/ MarketWatch illustration

JPMorgan increased loan-loss reserves amid warning from Jamie Dimon

JPMorgan Chase CEO Jamie Dimon [made one of the most widely cited comments of the current earnings season](#) when the bank increased its loan-loss reserves by \$810 million against an average loan book of \$1.4 trillion to cover a bad loan to bankrupt auto lender Tricolor.

"I probably shouldn't say this, but when you see one cockroach, there are probably more," Dimon said. "Everyone should be forewarned on this one."

But in the bank earnings updates that followed, the collective mantra by financials firms for analysts, investors and everyone else was that credit quality was good enough for the industry as a whole to reduce provisions for loan losses, which are the amounts added to loan-loss reserves each quarter to cover expected loan losses.

JPMorgan Chase did set aside more funds to cover bad loans. The bank's third-quarter provision for loan losses was 19% higher than it was during the second quarter and 11% above its year-earlier level. For Fifth Third Bancorp, the third-quarter provision was 14% above where it was in the second quarter and 64% higher than in the third quarter of 2024.

But overall, banks didn't increase their loan-loss provisions. They were cheered in that decision by analysts and investors who said that the loan losses at JPMorgan Chase and Fifth Third tied to the bankruptcy of auto dealer and lender Tricolor were isolated events and not part of a growing trend of defaults.

Banks may be incentivized not to set aside more money for bad loans. Rising provisions for credit losses can hurt stock prices, because the money for them comes directly from banks' profits. During particularly good times, banks may release provisions, which boosts their bottom line.

The reports of credit losses tied to the bankruptcies of Tricolor and car-parts company First Brands helped send the KBW Regional Banking Index down 6.3% on Oct. 16, which was its largest decline since April 3, when the index dropped 9.8% following President Donald Trump's April 2 "liberation day" tariff announcement. Before that, the index's worst day had been March 9, 2023, when it was down 6.4%. That was the day before Silicon Valley Bank was shut down by regulators.

The current message of confidence from banks stems from relatively low unemployment numbers and other positive economic indicators, despite a rise in layoffs this fall.

Also read: [ADP says businesses created 42,000 jobs in October — but the labor market is still not great](#)

"As a whole, we didn't see much change. Aggregate asset-quality metrics are stable," Johannes Moller, a bank-credit analyst at Moody's Ratings, told MarketWatch earlier this month. "Our baseline calls for a pretty benign economic outlook, but uncertainty remains high."

Regional banks remain under pressure

This undercurrent of perceived risks to banks continues to be a drag on stock prices of regional banks.

The Invesco KBW Regional Banking ETF, an exchange-traded fund that tracks the KBW Regional Banking Index by holding all 50 of its stocks, hasn't returned to record territory since setting an intraday high of \$70.14 on Jan. 18, 2022. The ETF's intraday high for 2025 was \$64.66 on Feb. 6, and it closed at \$57.84 on Thursday.

Regional-bank stocks briefly outperformed the S&P 500 over the summer, partly in anticipation of accelerating industry consolidation as well as on expectations that the Federal Open Market Committee would cut its target range for the federal-funds rate. Many regional banks are positioned to benefit quickly from the Fed's rate cuts. For most, net interest margins will widen as short-term rates decline because their deposits are positioned to reprice more quickly than their loan portfolios.

Also read: [Regional-bank stocks are catching up to larger rivals. How to play the sector from here.](#)

But since these isolated loan problems started cropping up in late summer and early fall, stocks in the sector have been under pressure.

Investor caution toward the sector spiked when a \$50 million loan-loss disclosure by Zions Bancorp [triggered the Oct. 16 stock selloff](#). Zions Bancorp's stock fell 13.1% that day, which was only two days after Dimon's remark about potential credit problems.

Bank stocks have seen some periods of volatility during recent years, as events such as the failures of Silicon Valley Bank, Signature Bank of New York and First Republic Bank of San Francisco in 2023 rekindled memories of the 2008 bankruptcy of Lehman Brothers and the financial crisis that followed.

Regional-bank stocks have yet to recover from their autumn losses.

Despite these systemic fears that can resurface, the U.S. banking industry appears to be in solid shape according to traditional metrics such as net charge-offs to average loans, capital ratios and returns on assets.

'There are risks and ... the fact that things are fine now doesn't mean they're guaranteed to be great forever.'

— Jeremy Barnum, chief financial officer of JPMorgan Chase

Investors are wary about any new hiccups in loan quality at regional banks, which rely more heavily on lending than larger, more diversified banks.

"There is still an overhang from 2023 that is likely driving investor sentiment and sensitivity within the marketplace to any negative news, even when underlying fundamentals, taken holistically, tell a different story," Moody's analyst Moller said. "There's a lot of nervousness in the market."

Matt Stucky, chief portfolio manager at Northwestern Mutual Wealth Management, said he remains more bullish toward larger banks, particularly JPMorgan Chase and Bank of

America, because of their larger loan portfolios, expanding market share and diverse business models.

While credit trends improved in the third quarter, investors still don't know how the fourth quarter and 2026 will shape up in terms of stock-market gains and employment trends, he said.

Banks typically set their provisions for loan losses based on the prevailing economic forecast, which includes a modest rise in unemployment in the coming months.

"If you have deviations from that forecast, they'll reserve more, and it could be a headwind" for bank profits, Stucky told MarketWatch.

Since an increase in unemployment has been expected for several months, banks have already worked out how this could affect their loan repayments and have made adjustments to their provisions accordingly, he said.

Even if the economy softens further, banks have been building up capital for years in the wake of the industry crisis in 2008-09, along with higher capital requirements and closer regulatory monitoring put in place after the Dodd-Frank banking reform legislation was signed into law by President Barack Obama in 2010.

A buildup of loan-loss reserves doesn't always mean trouble ahead. A bank may also put money into its reserves if its business is growing and it has more loans on its books. But banks typically increase their quarterly provisions for loan losses if they see storm clouds forming.

Banks' increased exposure to private credit as a potential risk

In recent weeks, fears about bank credit centered around bank loans to non-depository financial institutions, or money that traditional banks lend to nonbank borrowers such as Tricolor, which then use the "warehouse" money to make vehicle loans.

Warehouse lending and lending to NDFIs can be more opaque forms of debt that provide banks with higher returns than other loan types.

NDFI loans make up about 10.4% of the total loans by U.S. banks, which is about three times the level of a decade ago, Moller said. These loans now represent about \$1.2 trillion of exposure for U.S. banks, while exposure directly to private-credit lenders accounts for about a quarter of that, or \$300 billion, according to estimates from Moody's.

Banks have been leaning into private-credit deals, including NDFI loans, as a way to boost sluggish loan growth that's been trending below GDP in recent years.

At the end of 2024, banking regulators introduced enhanced reporting requirements for NDFI loan exposure for banks with over \$10 billion in assets.

Ahmed Ahmed, an assistant professor of finance at Babson College who studies bank balance sheets, said that private-credit and bank-credit conditions currently look good on paper, but underneath the surface there may be problems, such as potential collateral fraud.

“With private credit, you have a market where you don’t know how transactions are made or with what types of collateral,” Ahmed said in an interview. “It’s a very dark corner of financial markets, and banks are participating in that market.”

Ahmed sees a mismatch between the shorter-term capital adjustments that banks need to make in their balance sheets and the longer time horizon of some private-credit investments.

“Pension funds and insurance companies want to increase their yield on their portfolio through private credit, but it introduces a lot of illiquidity risks to this system,” Ahmed said.

Meanwhile, banks are enjoying a regulatory tailwind under [the enhanced supplementary leverage ratio for the biggest banks](#) now in the works.

And private credit and the promotion of alternative investment vehicles continues to expand on Wall Street, with more products aimed at wealthy individuals along with the usual client list of institutional investors.

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Chris Kotowski, an analyst at Oppenheimer, finds shares of alternative managers such as KKR, Ares Management and Blue Owl Capital attractive after their dip in October, which he attributed to irrational pessimism.

“We are not deniers of the existence of credit cycles, but students of them, and our studies tell us that we’re likely to remain in a strong credit environment,” he wrote in a research note.

The path of U.S. GDP and the plight of the country’s workforce will determine the overall credit strength for all forms of debt, but as Goldman Sachs CEO David Solomon said recently, “the real-time economy can shift very quickly.”

While upper-income people continue to thrive, the bank is closely watching consumers living paycheck to paycheck, who feel more pressured in an environment with 3% inflation, Solomon said in an Oct. 28 interview with Bloomberg.

An economic downturn would have a negative impact on bank credit, but the financial system is built to handle it, bankers have said this earnings season.

The best returns in long-cycle credit investing come “in the tough cycles when you have to restructure credits, you have to have more conviction to enter credits because you can earn higher returns,” Solomon said.

During JPMorgan’s analyst call on Oct. 14, Jeremy Barnum, the bank’s chief financial officer, said that for now, consumers remain resilient, with strong spending and lower-than-expected delinquency rates on credit cards and other loan products.

Slowing growth, market volatility and uncertainty among employers could potentially lead to worsening consumer credit performance, he said.

“I wouldn’t say we’re pounding the table with this view, but we’re just noting, as we always do, that there are risks and that the fact that things are fine now doesn’t mean they’re guaranteed to be great forever,” Barnum told analysts on Oct. 14.

The first signs of credit trouble usually crop up with consumer loans, specifically late credit-card repayments, and then with commercial loans, followed by mortgage loans.

“If people have jobs, banks will receive their loan payments for mortgage and auto loans on time,” said Northwestern Mutual’s Stucky.

For now, banks appear to be solid, he said.

“Collectively, across the board, banks faced concerns about loans to lower-end consumers and nonbank financial institutions,” Stucky said. “They reported much better than expedited credit trends.”