Banking Conditions Update

Joint Boards of Directors
January 12, 2023

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Net interest margins continue to rebound

Source: Reports of Condition and Income
Net income supported by improving margins

Return on Average Assets
Quarterly

Percent

- (0.25)
(0.50)
(0.75)
1.50
1.25
1.00
0.75
0.50
0.25

Sep-12  Sep-14  Sep-16  Sep-18  Sep-20  Sep-22

Community Banks
Regional Banks
Large Banks

Source: Reports of Condition and Income
Asset mix is shifting as loan growth increases

Change in Assets Since Year-End 2019

All US Banks

$ Billions

- 500 1,000 1,500 2,000 2,500


Loans* Cash Investment Securities

*Loan growth excludes Paycheck Protection Program (PPP) loans
Source: Reports of Condition and Income
Though balance sheets are hindered by unrealized losses

Asset Maturities
Community Banks

Unrealized Gains (Losses)
on Available-for-Sale Securities
Community Banks

Source: Reports of Condition and Income, Federal Reserve FOCUS Report
Funding structure is also shifting as deposit growth slows

Deposit Growth
Excluding Brokered Deposits, All US Banks

Non-Core Funds Growth
All US Banks

Source: Reports of Condition and Income
Impacts to capital, with divergence in tangible equity

Source: Reports of Condition and Income
Though asset quality remains stable, for now

Problem Loans and Allowance Levels
All US Banks, Percent of Total Loans (excluding PPP loans)

- 30-89 Days Past Due
- Nonaccrual and 90+ Days Past Due
- Allowance for Loan and Lease Losses

Source: Reports of Condition and Income
Crypto activity gaining interest

Common activities:

- Offering the ability to buy, hold, and sell crypto-assets, in response to significant customer demand

- Custody services for crypto-assets, a key element of which is safekeeping digital keys

- Lending against crypto-assets as collateral, enabling institutional clients to take leveraged positions in crypto-assets and crypto firms to borrow for working capital

- Deposits, loans, and payment services

- Working with other banks and/or non-banks to issue, distribute, or support a stablecoin
But regulation still evolving

2021
First coordinated messaging by federal regulators:
- Presidential Working Group Report on Stablecoins
- OCC Interpretive Letter #1179
- FBAs’ Joint Statement on Crypto Asset Policy Sprint Initiative and Next Steps

Begins to provide clarity on supervisory expectations and legal permissibility

2022
Supervisory guidance issued, establishes notification expectations:
- FDIC FIL-16-2022
- SR Letter/CA Letter 22-6

Presidential Executive Order on Ensuring Responsible Development of Digital Assets

2023 and beyond
Joint statement on crypto-asset risks to banking organizations
Continued need for clarity on permissibility
Draft bill: Bipartisan Stablecoin legislation?
More resources at kansascityfed.org

Community Banking Bulletin
Provides insights on trends or activities of primary interest to the community banking industry.

District Banking Conditions
Provides banking conditions for the nation and District, including data on earnings, expenses, assets, loans, and more.

Bank Capital Analysis Report
Provides a horizontal comparison of capital adequacy among banking organizations of different size and complexity.

Innovation
Financial Technology (Fintech) Innovation
Resources for engaging with the Federal Reserve on innovation-related matters.
Questions?
Definitions of Terms and Acronyms

- **Accumulated Other Comprehensive Income (AOCI):** An equity account that includes such items as unrealized gains and losses on certain securities.
- **Allowance for Loan and Lease Losses (ALLL):** An estimate of uncollectible amounts used to reduce the book value of loans and leases to the amount that a bank expects to collect.
- **Asset Maturities:** Uses the reported remaining maturity for fixed-rate loans and debt securities and next repricing date for floating-rate loans and debt securities.
- **Brokered Deposits:** A deposit that is obtained from or through the mediation or assistance of a deposit broker.
- **Commercial Banks:** Financial institutions which generally accept deposits from the public and make loans for the purpose of consumption and investment.
- **Community Bank:** A commercial bank with total assets under $10 billion. Community banks are financial institutions that primarily serve businesses and individuals in a small geographic area.
- **Cost of Funds:** A measure of the cost to acquire funds, calculated as total interest income divided by average earning assets.
- **Crypto-assets:** A digital representation of value that can be transferred, stored, or traded electronically.
- **Custody:** The legal access to or directly holding another’s assets.
- **Federal Home Loan Bank (FHLB):** The FHLBs are 11 regionally based, wholesale suppliers of lendable funds to financial institutions.
- **Investment Securities:** Includes held-to-maturity (HTM) and available-for-sale (AFS) securities. HTM securities are debt securities that an institution has the positive intent and ability to hold to maturity. Debt securities not categorized as trading or HTM are reported as AFS at fair value on the balance sheet.
Definitions of Terms and Acronyms

• **Large Bank**: A commercial bank with total assets greater than or equal to $100 billion. Large banks are financial institutions that usually have a national or global presence.

• **Net Interest Margin (NIM)**: A profitability measure which is calculated as net interest income (interest received less interest paid) divided by average earning assets.

• **Nonaccrual Loan**: A loan that is no longer accruing interest because the bank does not expect to receive principal or interest in full.

• **Other Borrowings**: Liabilities that include federal funds purchased, securities sold under agreements to repurchase, and other borrowed money.

• **Paycheck Protection Program (PPP)**: A loan program that originated from the Coronavirus Aid, Relief, and Economic Security (CARES) Act, intended to provide American small businesses with cash-flow assistance through 100 percent federally guaranteed loans.

• **Provisions**: An amount set aside to pay for probable, but uncertain, anticipated future losses.

• **Regional Bank**: A commercial bank with total assets greater than or equal to $10 billion, but less than $100 billion. Regional banks are financial institutions that are larger than community banks and typically operate in a specific region of the country.

• **Return on Average Assets (ROAA)**: A profitability measure which is calculated as net income divided by average total assets.

• **Stablecoin**: A type of digital asset designed to maintain a stable value relative to a national currency or other reference assets.

• **Tangible Common Equity**: A measure of a bank’s equity capital that excludes goodwill and other intangible assets.

• **Tier 1 Leverage Ratio**: Regulatory capital adequacy ratio that measures a bank’s core capital to its average tangible assets.

• **Unrealized Gains (Losses) on Available-for-Sale Securities**: The difference in the current market value from the stated book value.

• **Yield on Earning Assets**: A measure of how much income assets are generating, calculated as total interest income divided by average earning assets.