Supervision and Regulation Report

May 2024
The Federal Reserve System is the central bank of the United States. It performs five key functions to promote the effective operation of the U.S. economy and, more generally, the public interest.

The Federal Reserve

- **conducts the nation’s monetary policy** to promote maximum employment and stable prices in the U.S. economy;

- **promotes the stability of the financial system** and seeks to minimize and contain systemic risks through active monitoring and engagement in the U.S. and abroad;

- **promotes the safety and soundness of individual financial institutions** and monitors their impact on the financial system as a whole;

- **fosters payment and settlement system safety and efficiency** through services to the banking industry and U.S. government that facilitate U.S.-dollar transactions and payments; and

- **promotes consumer protection and community development** through consumer-focused supervision and examination, research and analysis of emerging consumer issues and trends, community economic development activities, and administration of consumer laws and regulations.

To learn more about us, visit [www.federalreserve.gov/aboutthefed.htm](http://www.federalreserve.gov/aboutthefed.htm).
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Preface

The Federal Reserve promotes the safety and soundness of individual financial institutions and monitors their impact on the financial system. It is responsible for supervising—monitoring, inspecting, and examining—certain financial institutions of varying size and complexity to ensure that they comply with rules and regulations, and that they operate in a safe and sound manner. The Federal Reserve supervises bank holding companies, savings and loan holding companies, the U.S. operations of foreign banking organizations, and state member banks.

The Federal Reserve Board publishes its semiannual Supervision and Regulation Report to inform the public of current banking conditions as well as provide transparency about its supervisory and regulatory policies and actions. Previous reports are available at https://www.federalreserve.gov/publications/supervision-and-regulation-report.htm.

For more information on how the Federal Reserve Board promotes the safety and soundness of individual financial institutions and the financial system see The Fed Explained: What the Central Bank Does at https://www.federalreserve.gov/aboutthefed/the-fed-explained.htm and visit the Supervision and Regulation web page on the Board’s public website at https://www.federalreserve.gov/supervisionreg.htm.
## Abbreviations

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<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>ACL</td>
<td>allowance for credit losses</td>
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<tr>
<td>AML</td>
<td>anti-money laundering</td>
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<tr>
<td>ASU</td>
<td>Accounting Standards Update</td>
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<tr>
<td>BHC</td>
<td>bank holding company</td>
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<td>BSA</td>
<td>Bank Secrecy Act</td>
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<td>BTFP</td>
<td>Bank Term Funding Program</td>
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<td>CA</td>
<td>Consumer Affairs</td>
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<tr>
<td>CAMELS ratings</td>
<td>Capital, Asset quality, Management, Earnings, Liquidity, and Sensitivity to market risk</td>
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<tr>
<td>CBLR</td>
<td>Community Bank Leverage Ratio</td>
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<td>CBO</td>
<td>community banking organization</td>
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<td>CDS</td>
<td>credit default swap</td>
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<td>CECL</td>
<td>current expected credit loss</td>
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<td>CET1</td>
<td>common equity tier 1</td>
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<tr>
<td>CFP</td>
<td>contingency funding plan</td>
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<tr>
<td>CRE</td>
<td>commercial real estate</td>
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<tr>
<td>C&amp;I</td>
<td>commercial and industrial</td>
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<tr>
<td>FASB</td>
<td>Financial Accounting Standards Board</td>
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<td>FBO</td>
<td>foreign banking organization</td>
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<tr>
<td>FDIC</td>
<td>Federal Deposit Insurance Corporation</td>
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<td>FFIEC</td>
<td>Federal Financial Institutions Examination Council</td>
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<tr>
<td>Fintech</td>
<td>financial technology</td>
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<tr>
<td>GAAP</td>
<td>generally accepted accounting principles</td>
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<td>G-SIB</td>
<td>global systemically important banking organization</td>
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<tr>
<td>IHC</td>
<td>intermediate holding company</td>
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<tr>
<td>IT</td>
<td>information technology</td>
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<tr>
<td>LBO</td>
<td>large banking organization</td>
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<td>LFBO</td>
<td>large and foreign banking organization</td>
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<td>LFI</td>
<td>large financial institutions</td>
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<tr>
<td>LISCC</td>
<td>Large Institution Supervision Coordinating Committee</td>
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<tr>
<td>Acronym</td>
<td>Description</td>
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<tr>
<td><strong>MRA</strong></td>
<td>Matters Requiring Attention</td>
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<td><strong>MRIA</strong></td>
<td>Matters Requiring Immediate Attention</td>
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<tr>
<td><strong>NBA</strong></td>
<td>nonbank assets</td>
</tr>
<tr>
<td><strong>RBO</strong></td>
<td>regional banking organization</td>
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<tr>
<td><strong>RRE</strong></td>
<td>residential real estate</td>
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<td><strong>SHC</strong></td>
<td>securities holding company</td>
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<td><strong>SLHC</strong></td>
<td>savings and loan holding company</td>
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<tr>
<td><strong>SLOOS</strong></td>
<td>Senior Loan Officer Opinion Survey</td>
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<tr>
<td><strong>SMB(s)</strong></td>
<td>state member bank(s)</td>
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<tr>
<td><strong>SR</strong></td>
<td>Supervision and Regulation</td>
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<tr>
<td><strong>U.S. G-SIB</strong></td>
<td>global systemically important banking organization headquartered in the United States</td>
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<td><strong>wSTWF</strong></td>
<td>weighted short-term wholesale funding</td>
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</table>
Executive Summary

The banking system remains sound and resilient. Most banks continue to report capital and liquidity levels above applicable regulatory requirements. Aggregate commercial bank deposit levels stabilized in the second half of 2023 and slightly increased in early 2024. Asset quality remains sound overall. However, delinquency rates for some commercial real estate loans and some consumer loans have increased to above pre-pandemic levels. Banks have boosted the allowance for credit losses in anticipation of further deterioration in asset quality.

The Federal Reserve is focused on improving the speed, force, and agility of supervision, as appropriate. This includes ensuring supervisory actions are commensurate with a banking organization’s size, risk, and complexity. The Federal Reserve continues to closely monitor risks to the banking sector, including credit, interest rate, and liquidity risks.

This report focuses on developments in three areas:

1. Banking System Conditions provides an overview of the financial condition of the banking sector.
2. Regulatory Developments outlines the Federal Reserve’s recent regulatory policy work.
3. Supervisory Developments highlights the Federal Reserve’s current supervisory programs and priorities.
Banking System Conditions

The banking system remains sound and resilient. Most banks continue to report capital and liquidity levels above applicable regulatory requirements. Deposits have increased overall since the last report.\(^1\) Still, some banks face challenges navigating changes in depositor behavior, higher funding costs, and reduced market values for investment securities. Asset quality generally remains sound. However, commercial real estate (CRE) and consumer loan delinquencies have been increasing. Earnings have declined as banks have increased loan loss provisions and incurred higher funding costs. The special assessment by the Federal Deposit Insurance Corporation (FDIC) also contributed to the decline.

Capital Has Increased

Regulatory capital increased in 2023. In aggregate, banks added $76 billion in common equity tier 1 (CET1) capital between year-end 2022 and year-end 2023. Over this period, their CET1 capital ratio increased nearly 50 basis points (Figure 1).

An alternative capital measure, the tangible common equity (TCE) ratio, also increased. However, it remained below pre-pandemic levels. The TCE ratio is similar to the CET1 capital ratio in that both ratios exclude intangible items such as goodwill; however, the TCE ratio does not account for the riskiness of assets but does include changes in the fair value of available-for-sale securities for all banks.\(^2\) Substantial declines in the fair value of securities can weaken a bank’s ability to meet unexpected liquidity needs. Some banks continue to report large fair value losses on investment securities resulting from prior interest rate increases.

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2 Accounting standards do not require banks to reflect declines in the fair value of held-to-maturity securities within equity capital. However, for held-to-maturity securities that were transferred from the available-for-sale category, declines in fair value that existed at the date of the transfer are reported within equity capital.
Liquidity Conditions are Stable

Liquid assets remained above their 10-year average throughout 2023.\(^3\) As a share of total assets, liquid asset levels were relatively flat between year-end 2022 and year-end 2023. A decline in the value of securities on bank balance sheets was mostly offset by an increase in cash holdings over this period (figure 2). Security balances declined due to both lower fair values and reduced holdings by banks.

Aggregate deposits were largely stable in the second half of 2023 and steadily increased in the first three months of 2024. In January 2024, deposits at commercial banks rose above $17.5 trillion for the first time since the banking stresses of March 2023 (figure 3).

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At the same time, banks increased their reliance on higher cost wholesale funding sources. After falling to historic lows in early 2022, wholesale funding rose to 21.6 percent of total assets at year-end 2023, more in line with pre-pandemic levels (figure 4). As scheduled, the Bank Term Funding Program ceased extending new loans on March 11, 2024, and the size of the program has begun to decline.\(^5\)\(^6\)

Banks have improved their operational readiness to access the discount window. Since the banking stresses of March 2023, the amount of collateral pre-positioned at the discount window has increased significantly and is now nearly $3 trillion. Over 5,000 banks and credit unions are signed up to use the discount window, of which nearly 3,000 have collateral pledged.\(^7\)

### Loan Growth Has Slowed with Delinquencies Increasing in Some Sectors

Loan growth is still positive but has slowed from a rapid pace the year before. Both weaker loan demand and tighter lending standards contributed to the slowdown. Loan growth in most sectors was modest in 2023. A major exception was the credit card sector. Credit card balances

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increased to a historic high at the end of 2023, despite tightened lending standards and fewer credit line increases at large banks.¹⁰

Overall asset quality remains generally sound. The total loan delinquency rate was below one percent at year-end 2023, as the delinquency rate for commercial and industrial (C&I) loans was relatively stable and the delinquency rate for residential real estate (RRE) steadily declined in 2023. However, delinquency rates are rising in CRE and some consumer sectors. The delinquency rate for consumer loans rose above one percent for the first time since the first quarter of 2020, and the delinquency rate for CRE loans increased to 0.9 percent, a five-year high (figure 5).

The rise in CRE delinquencies was largely due to loans secured by nonowner-occupied nonfarm nonresidential properties in banks with at least $100 billion in total assets. Nonowner-occupied nonfarm nonresidential properties include hotels, offices, retail stores, warehouse facilities, and other types of business property used as collateral. At the large banks, office loans showed the greatest delinquency rate increase among property types, particularly in metropolitan areas (figure 6). Reduced demand for office space and higher interest rates adversely affected office loan performance.¹¹ While banks with total assets of less than $100 billion have lower CRE delinquency rates than large banks, they have a greater percentage of their total loans exposed to the CRE sector.


The delinquency rate for consumer loans was driven higher in 2023 by the credit card and auto loan sectors (figure 7). The credit card loan delinquency rate reached 1.7 percent at year-end 2023, its highest level in the last five years. In addition, the share of borrowers carrying forward all or some portion of their credit card balance to the next billing cycle has increased. The delinquency rate for auto loans increased in 2023 and now exceeds pre-pandemic levels.\textsuperscript{12} Auto loans originated prior to the pandemic by banks with total assets over $100 billion have performed worse than newer loans, partially reflecting a tightening of lending standards for the newer loans.

Earnings Have Declined, in Part Due to Nonrecurring Expenses

Return on average assets and return on equity were near their 10-year averages in the first three quarters of 2023. The FDIC special assessment and other nonrecurring expenses in the fourth quarter led to a sharp decline in both earnings metrics (figure 8).\textsuperscript{13,14} Excluding the FDIC special assessment, both earnings metrics would still have declined, but by a smaller amount.

Net interest margin measures the difference between interest income and interest expense, relative to interest earning assets. Aggregate net interest margin declined slightly in 2023 as interest expense increased faster than interest income. Interest expense rose quickly in 2023 as banks paid more for deposits and used more wholesale funding.


\textsuperscript{14} Other nonrecurring expenses included goodwill impairments, Bloomberg Short-term Bank Yield Index cessation charges, Foreign Exchange devaluations, and severance costs.
Aggregate loan loss provisions also increased in 2023 (figure 9). Large banks have increased provisions amid credit quality concerns in the CRE and consumer loan sectors. Higher losses from the sale of investment securities also contributed to the decline in earnings.

**Market Indicators Have Improved**

Market assessments of bank risk, including the market leverage ratio and credit default swap (CDS) spreads, provide a forward-looking assessment of the strength of the banking system. The market leverage ratio measures a bank’s financial position based on the ratio of its market capitalization to the sum of market capitalization and the book value of liabilities. A lower stock price reduces the market leverage ratio, indicating lower market confidence in a bank’s financial strength. Conversely, higher stock prices produce a higher ratio, reflecting a higher degree of confidence in a bank’s financial strength. As a complement to the market leverage ratio, CDS spreads track the price of insurance against a default by a given bank. If a bank’s CDS spread increases, it means the market has lower confidence in the bank’s creditworthiness. Lower CDS spreads indicate higher market confidence in a bank’s creditworthiness.\(^{15}\)

The average market leverage ratio and average CDS spread for the largest banks moved in directions consistent with an improvement in investor sentiment since the last report (figure 10).

**First Quarter 2024 Earnings at Large Firms**

This section provides a recap of first quarter 2024 earnings results for 23 large banking firms (“large banks”).\(^{16}\) While such metrics are indicative, it should be noted that the sample may not necessarily be representative of the entire banking sector.

In the first quarter of 2024, large banks reported healthy financial performance. Aggregate large bank profitability, as measured by return on equity, was 12 percent, compared to 5 percent in the

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\(^{15}\) See the appendix for additional information on the market indicators.

\(^{16}\) The sample includes Ally Financial Inc.; American Express Company; Bank of America Corporation; The Bank of New York Mellon Corporation; Capital One Financial Corporation; The Charles Schwab Corporation; Citigroup Inc.; Citizens Financial Group, Inc.; Discover Financial Services; Fifth Third Bancorp; The Goldman Sachs Group, Inc.; Huntington Bancshares Incorporated; JPMorgan Chase & Co.; KeyCorp; M&T Bank Corporation; Morgan Stanley; Northern Trust Corporation; The PNC Financial Services Group, Inc.; Regions Financial Corporation; State Street Corporation; Truist Financial Corporation; U.S. Bancorp; and Wells Fargo & Company. Data is unadjusted for mergers and acquisitions.
fourth quarter of 2023 and 13 percent in the first quarter of 2023. In the first quarter of 2024, large banks reported higher quarter-over-quarter earnings due to higher capital market and investment management fee revenues, lower nonrecurring costs, and smaller credit loss provisions, which were partially offset by lower net interest income.

At most large banks, both the nonperforming loan rate and loan loss rate increased quarter-over-quarter. Credit loss allowances as a percentage of loans remained relatively stable with fourth quarter 2023 levels. Large banks continued to indicate that credit loss allowances will be sufficient to cover potential future loan losses, including loans in the office commercial real estate and credit card categories.

The aggregate CET1 capital ratio for large banks approximated 12 percent on March 31, 2024, in line with the level on December 31, 2023.
Regulatory Developments

The Federal Reserve has taken several policy actions since the publication of the November 2023 Supervision and Regulation Report (see table 1). All Supervision and Regulation (SR) and Consumer Affairs (CA) letters are available on the Federal Reserve Board’s public website.17

<table>
<thead>
<tr>
<th>Date issued</th>
<th>Rule/guidance</th>
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Third-Party Risk Management: A Guide for Community Banks

To supplement the broader third-party risk-management guidance issued in June 2023, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency issued a third-party risk-management guide for community banks in May 2024.18 The guide is intended to assist community banks when developing and implementing their third-party risk-management practices. The guide is a supplementary resource consistent with other similar tools that have been provided to community banks focused on managing various aspects of these relationships.19 The guide provides potential considerations, resources, and examples through each stage of the third-party risk-management life cycle. The guide also references potential considerations and resources for related governance practices.

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17 The Federal Reserve publishes SR and CA letters to address significant policy and procedural matters related to the Federal Reserve System’s safety-and-soundness and consumer compliance supervisory responsibilities, respectively. SR letters are available on the Board’s public website at https://www.federalreserve.gov/supervisionreg/srletters/srletters.htm, and CA letters are available on the Board’s public website at https://www.federalreserve.gov/supervisionreg/caletters/caletters.htm.


Economic Growth and Regulatory Paperwork Reduction Act of 1996

In February 2024, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (federal bank regulatory agencies) announced the first of a series of requests for comment to reduce regulatory burden.\(^20\) The Economic Growth and Regulatory Paperwork Reduction Act of 1996 requires the Federal Financial Institutions Examination Council and federal bank regulatory agencies to review their regulations every 10 years to identify any outdated or otherwise unnecessary regulatory requirements for their supervised institutions. The agencies divided their regulations into 12 categories and will be soliciting comments over the next two years. This first request solicits feedback on three categories: Applications and Reporting, Powers and Activities, and International Operations. Comments on the relevant regulations will be accepted for 90 days after publication in the Federal Register.

Supervisory Developments

This section provides an overview of recent supervisory efforts to assess institutions’ safety and soundness and compliance with laws and regulations. Supervisory approaches and priorities differ by a financial institution’s size and complexity. The subsections below discuss developments separately for large financial institutions with assets of $100 billion or more, and community and regional banking organizations with assets of less than $100 billion.

The Federal Reserve is responsible for overseeing the implementation of certain laws and regulations relating to consumer protection and community reinvestment. The scope of the Federal Reserve’s supervisory jurisdiction varies based on the consumer law or regulation and on the asset size of the state member bank. Consumer-focused supervisory work is designed to promote a fair and transparent marketplace for financial services and to ensure supervised institutions comply with applicable federal consumer protection laws and regulations.

More information about the Federal Reserve’s consumer-focused supervisory program can be found in the Federal Reserve’s 109th Annual Report 2022.21

Federal Reserve Supervision

The Federal Reserve conducts examinations to evaluate a banking organization’s activities, risk management, and financial condition.22 Examinations include assessments of capital adequacy, asset quality, earnings strength and quality, liquidity position and funding sources, sensitivity to interest rate risks, and the quality of board and management oversight. The Federal Reserve may also decide whether to further focus examinations on supervised institutions’ known and potential risks.

If supervisors find issues with a bank’s risk management or financial condition, they provide direction and require the bank to correct its weaknesses.23 This direction takes the form of confidential supervisory findings called “Matters Requiring Attention” (MRAs) and, for more significant issues that must be corrected on a priority basis, “Matters Requiring Immediate Attention” (MRIAs). These findings are communicated to a banking organization’s management and board of directors.

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23 Supervisors includes both commissioned examiners (Federal Reserve staff who have been commissioned as an examiner) and subject matter experts that provide support during examinations and off-site monitoring.
in a written exam or inspection report. If a bank does not address these supervisory findings or if the findings are significant enough to pose a threat to a bank’s safety and soundness, supervisors may lower the bank’s supervisory ratings or pursue an enforcement action against the bank.

Supervisory ratings, which are confidential, provide an assessment of a bank’s risk management and financial condition based on examination results, supervisory findings, and other information gathered throughout the year. These ratings reflect supervisors’ overall judgment of a bank’s safety and soundness. Supervisory ratings are generally issued once a year for larger banks and every 18 months for smaller banks but may also be issued on an interim basis if circumstances warrant.24

**Supervised Institutions**

The Federal Reserve supervises bank holding companies, savings and loan holding companies, state member banks, and foreign banking organizations operating in the United States. The Federal Reserve follows a risk-focused approach by scaling supervisory work to the asset size and complexity of an institution:

- The Large Institution Supervision Coordinating Committee (LISCC) program supervises firms that pose elevated risk to U.S. financial stability.
- The Large and Foreign Banking Organization (LFBO) program supervises U.S. firms with total assets of $100 billion or more and all foreign banking organizations operating in the United States regardless of asset size.
- The Regional Banking Organization (RBO) program supervises U.S. firms with total assets between $10 billion and $100 billion.
- The Community Banking Organization (CBO) program supervises U.S. firms with less than $10 billion in total assets.

Table 2 provides an overview of Federal Reserve supervised organizations by portfolio, including the number of institutions and total assets in each portfolio.

**Current Supervisory Priorities**

In 2023, the Federal Reserve intensified supervisory efforts to assess banks’ preparedness for managing liquidity and credit risks. The Federal Reserve initiated continuous monitoring for a small number of firms with risk profiles vulnerable to funding pressures. The monitoring assessed the adequacy of firms’ liquidity and interest rate risk management. Banks are expected to have pru-

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dent liquidity risk-management practices and to regularly test their ability to access multiple sources of contingent funding.

Given increased delinquencies in certain loan sectors, credit risk continues to be a supervisory priority. Supervisors are closely monitoring underwriting standards and loan quality. In addition, for CRE-concentrated state member banks, supervisors are conducting in-depth examinations to ensure concentrated banks are exercising strong risk-management practices.

Cybersecurity risk remains a priority. Supervisors are conducting examinations to ensure banks have adequate controls and resilience to protect their data and operations against cybersecurity threats.

**The Novel Activities Supervision Program**

The Novel Activities Supervision Program is continuing its work with existing Federal Reserve supervisory teams to strengthen the oversight of banking organizations engaged in novel activities.

<table>
<thead>
<tr>
<th>Portfolio</th>
<th>Definition</th>
<th>Number of institutions</th>
<th>Total assets ($ trillions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large Institution Supervision Coordinating Committee (LISCC)</td>
<td>Eight U.S. global systemically important banks (G-SIBs)</td>
<td>8</td>
<td>14.9</td>
</tr>
<tr>
<td>State member banks (SMBs)</td>
<td>SMBs within LISCC organizations</td>
<td>4</td>
<td>1.2</td>
</tr>
<tr>
<td>Large and foreign banking organizations (LFBOs)</td>
<td>Non-LISCC U.S. firms with total assets $100 billion and greater and FBOs</td>
<td>170</td>
<td>10.5</td>
</tr>
<tr>
<td>Large banking organizations (LBOs)</td>
<td>Non-LISCC U.S. firms with total assets $100 billion and greater</td>
<td>18</td>
<td>5.1</td>
</tr>
<tr>
<td>Large FBOs (with IHC)</td>
<td>FBOs with combined U.S. assets $100 billion and greater</td>
<td>10</td>
<td>2.9</td>
</tr>
<tr>
<td>Large FBOs (without IHC)</td>
<td>FBOs with combined U.S. assets $100 billion and greater</td>
<td>7</td>
<td>1.3</td>
</tr>
<tr>
<td>Small FBOs (excluding rep offices)</td>
<td>FBOs with combined assets less than $100 billion</td>
<td>103</td>
<td>1.1</td>
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<tr>
<td>Small FBOs (rep offices)</td>
<td>FBO U.S. representative offices</td>
<td>32</td>
<td>0.0</td>
</tr>
<tr>
<td>State member banks</td>
<td>SMBs within LBO organizations</td>
<td>9</td>
<td>1.1</td>
</tr>
<tr>
<td>Regional banking organizations (RBOs)</td>
<td>Total assets between $10 billion and $100 billion</td>
<td>105*</td>
<td>2.8</td>
</tr>
<tr>
<td>State member banks</td>
<td>SMBs within RBO organizations</td>
<td>39</td>
<td>1.0</td>
</tr>
<tr>
<td>Community banking organizations (CBOs)</td>
<td>Total assets less than $10 billion</td>
<td>3,452**</td>
<td>3.0</td>
</tr>
<tr>
<td>State member banks</td>
<td>SMBs within CBO organizations</td>
<td>654</td>
<td>0.7</td>
</tr>
<tr>
<td>Insurance and commercial savings and loan holding companies (SLHCs)</td>
<td>SLHCs primarily engaged in insurance or commercial activities</td>
<td>5 insurance 4 commercial</td>
<td>0.5</td>
</tr>
</tbody>
</table>

* Includes 104 holding companies and 1 state member bank that does not have a holding company.
** Includes 3,401 holding companies and 51 state member banks that do not have holding companies.
and to help foster responsible innovation. Supervisors are engaging with institutions to assess novel activities, their associated risks, and the effectiveness of controls to manage these risks. Program staff are also monitoring trends in novel activities at banks, the broader crypto-asset and fintech market, and other novel material developments in this space.

**Large Financial Institutions**

This section of the report discusses the supervisory approach for large financial institutions—namely, U.S. firms with total assets of $100 billion or more, and foreign banking organizations with combined U.S. assets of $100 billion or more. These firms are either within the LISCC portfolio or the LFBO portfolio. Large financial institutions are subject to regulatory requirements that are tiered to the risk profiles of these firms. The appendix provides an overview of key regulatory requirements.

Supervisory efforts for large financial institutions focus on four components:

1. Capital planning and positions,
2. Liquidity risk management and positions,
3. Governance and controls, and
4. Recovery and resolution planning.26

**The Financial Condition of Large Financial Institutions**

Large financial institutions’ capital positions remain above minimum regulatory ratios. However, declines in the fair value of securities have weighed on their tangible equity. In 2023, large financial institutions increased capital ratios, primarily through optimizing risk weighted assets and reducing share repurchases. Large financial institutions’ aggregate CET1 capital ratio increased to 12.7 percent as of December 31, 2023, from 12.3 percent as of June 30, 2023.

Large financial institutions’ profitability, as measured by return on average assets and return on equity, declined in the fourth quarter. The decline was largely driven by the FDIC special assessment and one-time costs incurred in the fourth quarter.27,28 Excluding these costs, profitability was in line with 2022 levels. Net interest margins remained relatively flat.

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28 One-time charges included goodwill impairments, Bloomberg Short-term Bank Yield Index cessation charges, Foreign Exchange devaluations, and severance costs.
At year-end 2023, total loan delinquencies increased to near pre-pandemic levels, driven by CRE and credit cards loans. Large financial institutions continued to increase allowances for credit losses primarily due to a weak outlook for the CRE office and credit card portfolios.

Liquidity positions remain substantially above regulatory requirements. These positions have generally declined from their pandemic peaks but stabilized to pre-pandemic levels.

**Trends in Supervisory Ratings and Findings**

Federal Reserve supervisors summarize their assessments of large financial institutions using the LFI rating system. The LFI rating system evaluates whether a firm possesses sufficient financial and operational strength and resilience to maintain safe-and-sound operations and comply with laws and regulations, including those related to consumer protection, through a range of conditions. It includes three components: (1) capital planning and positions; (2) liquidity risk management and positions; and (3) governance and controls. Each component is rated based on a four-point non-numeric scale: Broadly Meets Expectations, Conditionally Meets Expectations, Deficient-1, and Deficient-2. A firm is considered to be in satisfactory condition if all of its component ratings are “Broadly Meets Expectations” or “Conditionally Meets Expectations.”

As of December 31, 2023, two-thirds of large financial institutions were meeting supervisory expectations with respect to the (1) capital positions and planning or (2) liquidity risk management and positions components. However, supervisors have found weaknesses in interest rate risk and liquidity risk-management practices at several large financial institutions. Some large financial institutions continued to show weaknesses in governance and controls related to operational resilience, cybersecurity, and BSA/AML compliance. As a result, only about one-third of the large financial institutions had satisfactory ratings across all three LFI rating components (figure 11).

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Outstanding supervisory findings at large financial institutions have increased in the second half of 2023, which contributes to the higher percentage of firms being rated less than satisfactory (figure 12). Supervisory findings related to weaknesses in liquidity and interest rate risk-management practices increased. Governance and controls findings represent approximately two-thirds of outstanding issues (figure 13).

Supervisory Focus

Supervisors conduct firm-specific examinations and horizontal reviews to assess large financial institutions’ resilience and risk-management practices. Horizontal review allows supervisors to compare risk-management practices, identify gaps in practices, and promote sound practices across firms.

Throughout 2023, the Federal Reserve conducted examinations and closely monitored liquidity positions and risk management at large financial institutions. This included reviewing recent deposit trends, deposit and liability management strategies, liquidity risk-management practices, access to secured funding, liquidity stress test projections related to deposits, and liquidity buffer composition.

Supervisors completed examinations to assess interest rate risk-management practices across several large financial institutions. The exams assessed the adequacy of firms’ risk-management
processes to identify, measure, monitor, and, as needed, mitigate interest rate and related liquidity risks.

Supervisors conducted examinations to monitor and assess credit risk, as asset quality has deteriorated for some loan types. Some large financial institutions reported higher loan losses for CRE and credit card loans and have generally increased provisions for credit losses. Recent examinations reviewed loan quality, firms’ internal risk reporting, loss forecasting, risk management, and reserves for credit loss adequacy. In addition, supervisors have assessed the level and quality of loans to nonbank financial institutions, given a substantial increase in lending to this sector in recent years.

Supervisors examined cybersecurity practices across large financial institutions as cyber threats persisted. The examinations assessed firms’ capabilities to identify, measure, monitor, and protect against cybersecurity risk.

See below for additional detail on large financial institutions’ supervisory priorities for the coming months.

**Large Financial Institution Supervisory Priorities**

**Capital**
- interest rate risk
- market and counterparty risk
- consumer and commercial credit, including commercial real estate
- firm remediation efforts on previous supervisory findings

**Liquidity**
- internal liquidity stress tests, including
  - changes to deposit stress testing segmentation and runoff rate assumptions
  - highly liquid asset composition frameworks and monetization assumptions
- firm remediation efforts on previous supervisory findings
- intraday liquidity monitoring and risk-management practices

**Governance and Controls**
- operational resilience including cybersecurity
- novel banking and information technology risks
- third-party vendor management
- firm remediation efforts on previous supervisory findings
Recovery and Resolution Planning

- recovery and resolution planning, including biannual resolution plan review for the G-SIBS
- remediation and follow-up on resolution plan shortcomings and exam findings, as necessary
- international coordination among global supervisors

Community and Regional Banking Organizations

This section of the report discusses the financial condition and supervisory approach for banking organizations with assets of less than $100 billion, including community banking organizations (CBOs), which have less than $10 billion in total assets, and regional banking organizations (RBOs), which have total assets between $10 billion and $100 billion.

The Financial Condition of CBOs and RBOs

CBOs and RBOs generally remain in sound financial condition, with most banks continuing to report strong capital positions. The aggregate tier 1 leverage ratio increased in 2023, as capital growth outpaced asset growth. The aggregate TCE ratio also increased slightly year-over-year, as the fair value of securities held by banks increased.

Earnings of CBOs and RBOs declined in 2023. Higher funding costs and weaker loan growth compressed net interest margins. For RBOs, higher provisions and noninterest expense, partially attributed to the FDIC special assessment, also contributed to the decline in earnings.

Asset quality generally remains sound. Problem loan levels remain low overall. The total loan delinquency rate increased slightly in 2023. Some banks reported deteriorating CRE loan performance.

Liquidity positions for most CBOs and RBOs are satisfactory. The share of uninsured deposits declined to a level more comparable to pre-pandemic levels. However, challenges remain for some banks. The aggregate ratio of wholesale funding to total assets increased in 2023. Some banks continue to rely heavily on wholesale funding sources that are often more costly and less stable than deposits. Federal Reserve supervisors are closely monitoring liquidity trends and adequate access to contingency funding.

Trends in Supervisory Ratings and Findings

The Federal Reserve and the other federal and state banking agencies utilize the Uniform Financial Institution Rating System (referred to as “CAMELS”) to present the supervisor’s conclusions regarding the overall condition of the bank. The CAMELS composite rating represents an overall appraisal of six key assessment components covered under the CAMELS rating system: Capital adequacy, Asset quality, Management, Earnings, Liquidity, and Sensitivity to market risk.
For the inspection of a holding company with less than $100 billion in total consolidated assets, the Federal Reserve utilizes the RFI rating system to present the supervisor’s conclusions regarding the overall condition of these holding companies. The RFI composite rating represents an overall assessment of three components covered under the RFI rating system: Risk Management, Financial Condition, and Impact of the non-depository entities on the subsidiary depository institutions.

The CAMELS and RFI rating systems are assigned based on a “1 to 5” numeric scale. A “1” numeric rating indicates the highest rating, strongest performance and practices, and least degree of supervisory concern. A “5” numeric rating indicates the lowest rating, weakest performance, and highest degree of supervisory concern. Banks and holding companies that are rated “1” or “2” are generally in satisfactory condition, while banks that are rated “3,” “4,” or “5” are in less-than-satisfactory condition.

The majority of CBOs and RBOs remain in satisfactory condition with effective risk-management practices (figure 14). However, supervisory ratings downgrades have increased due in part to weaknesses in interest rate and liquidity risk-management practices.

The number of outstanding supervisory findings has increased in 2023 (figure 15). For CBOs, the most cited supervisory issues relate to IT/operational risk, management/risk-management weaknesses, and credit risk (figure 16). For RBOs, the most cited supervisory findings relate to IT/operational risk, management/risk management, and market/liquidity risk (figure 17).

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Supervisor Focus

During 2023, the Federal Reserve intensified monitoring of CBOs and RBOs that appeared most vulnerable to funding pressures. Where appropriate, Federal Reserve supervisors required bank management to improve access to contingency funding, increase liquid asset buffers, and reassess deposit outflow assumptions in contingency funding plans. For certain banks, Federal Reserve supervisors assessed their ability to mitigate risk from deposit concentrations and high levels of uninsured deposits. Supervisors also worked to ensure that those banks update their contingency funding plans as needed.

Federal Reserve supervisors are closely monitoring CRE market developments and credit risks at banks with large CRE credit concentrations. Supervisors expect banks with larger CRE credit concentrations to have robust risk-management practices and to quantify the impact of changing economic conditions on their earnings, asset quality, and capital. In 2023 at certain
RBOs, Federal Reserve supervisors conducted supervisory work to assess risk-management processes and stress test individual loans and loan portfolios.

See below for additional detail on CBO and RBO supervisory priorities for the coming months.

**CBO and RBO Supervisory Priorities**

**Credit Risk**
- high-risk loan portfolios, credit risk management, and debt service coverage capacity in a changing interest rate environment
- credit concentrations, particularly in CRE loan portfolios
- impact of rising capitalization (cap) rates and real estate valuation uncertainty
- adequacy of an institution’s allowance and provisioning methodology

**Liquidity Risk**
- contingency funding plans
- liquidity coverage of uninsured deposits

**Other Financial Risks**
- capital adequacy, and the potential impact of deteriorating credit quality metrics of certain loan sectors on earnings and capital
- interest rate risk and sensitivity risk
- declines in the fair value of securities and low tangible common equity levels

**Operational Risk**
- information technology and cybersecurity preparedness
- fintech and banking-as-a-service activities
- third-party risk management
Appendix: Data Sources and Terms

Data Sources

The Supervision and Regulation Report includes data both on institutions supervised by the Federal Reserve System and some institutions outside Federal Reserve supervision. The report reflects data through April 1, 2024. This appendix details these sources.

FFIEC Call Reports

The FFIEC Consolidated Reports of Condition and Income, also known as the Call Report, is a periodic report that is required to be completed by every national bank, state member bank, insured nonmember bank, and savings association as of the last day of each calendar quarter. The details required to be reported depend on the size of the institution, the nature of the institution’s activities, and whether it has foreign offices. Call Report data are a widely used source of timely and accurate financial data regarding a bank’s financial condition and the results of its operations. The data collected on the Call Report are used to monitor the condition, performance, and risk profiles of reporting institutions individually and altogether.

FR Y-9C

The Consolidated Financial Statement for Holding Companies, also known as the FR Y-9C report, collects basic financial data from domestic bank holding companies (BHCs), savings and loan holding companies (SLHCs), U.S. intermediate holding companies of foreign banking organizations (U.S. IHCs), and securities holding companies (SHCs). Initiatives to reduce reporting costs for firms led to increases in the minimum asset size thresholds for reporting from $500 million to $1 billion, and from $1 billion to $3 billion, effective March 2015 and September 2018, respectively. In addition, BHCs, SLHCs, U.S. IHCs, and SHCs meeting certain criteria may be required to file this report, regardless of size. However, when such BHCs, SLHCs, U.S. IHCs, or SHCs own or control, or are owned or controlled by, other BHCs, SLHCs, U.S. IHCs, or SHCs, only top-tier holding companies must file this report for the consolidated holding company organization. The information contained in the report is as of the last day of each calendar quarter.

FR Y-14Q

The FR Y-14Q report is part of the Capital Assessments and Stress Testing information collection (FR Y-14). The FR Y-14 data collection is used to assess the capital adequacy of large firms using forward-looking projections of revenue and losses and to support supervisory stress test models and continuous monitoring efforts as well as to inform the Federal Reserve’s operational decision-
making and implement the Dodd-Frank Wall Street Reform and Consumer Protection Act (2010). The FR Y-14Q collects detailed data on BHCs’, IHCs’, and SLHCs’ various asset classes, capital components, and categories of pre-provision net revenue.

**H.8 Assets and Liabilities of Commercial Banks in the United States**

The H.8 release provides an estimated weekly aggregate balance sheet for all commercial banks in the United States. The H.8 estimates are primarily based on the FR 2644 reporting form—reported weekly by a voluntary authorized panel of 850 domestically chartered banks and foreign-related institutions—and quarterly Consolidated Reports of Condition and Income for those commercial banks that are not included in the FR 2644 panel.

**Notes on Data Sources and Terms**

**CAMELS Ratings**

Following an examination of a commercial bank, the examiner’s conclusions regarding the overall condition of the bank are summarized in a composite rating assigned in accordance with guidelines provided under the Uniform Financial Institution Rating system (referred to as “CAMELS”). The composite rating represents an overall appraisal of six key assessment areas (components) covered under the CAMELS rating system: Capital, Asset quality, Management, Earnings, Liquidity, and Sensitivity to market risk.

In addition to and separate from the interagency Uniform Financial Institutions Rating System, the Federal Reserve assigns a risk-management rating to all SMBs. The summary, or composite, rating, as well as each of the assessment areas, including risk management, is delineated on a numerical scale of 1 to 5, with 1 being the highest or best possible rating. Thus, a bank with a composite rating of 1 requires the lowest level of supervisory attention while a 5-rated bank has the most critically deficient level of performance and, therefore, requires the highest degree of supervisory attention.

When appraising the six key assessment areas and assigning a composite rating, the examiner weighs and evaluates all relevant factors for downgrades and upgrades of supervisory ratings.

**Current Expected Credit Losses Methodology (CECL)**

In 2016, the Financial Accounting Standards Board (FASB) announced significant changes to credit loss accounting under U.S. generally accepted accounting principles (GAAP). Refer to Accounting Standards Update (ASU) No. 2016-13, Financial Instruments—Credit Losses, Topic 326, Measurement of Credit Losses on Financial Instruments.
CECL replaced the incurred loss methodology for financial assets measured at amortized cost. For these assets, CECL requires banking organizations to recognize lifetime expected credit losses. Further, banking organizations are required to incorporate reasonable and supportable forecasts in developing their estimate of lifetime expected credit losses, while also considering past events and current conditions.

Supervised institutions that are SEC filers, excluding smaller reporting companies, were required to adopt CECL on January 1, 2020. All other institutions were required to implement CECL by January 1, 2023. For additional information, refer to the Federal Reserve’s CECL Resource Center – CECL Resource Center (https://www.supervisionoutreach.org/).

**Commercial Real Estate Loans**

Commercial real estate loans are the sum of construction, land development, and other land loans; loans secured by multifamily residential properties; and loans secured by nonfarm nonresidential properties.

Note: H.8 commercial real estate data include loans secured by farmland.

**Common Equity Tier 1 (CET1)**

Common equity capital is currently evaluated using a CET1 capital ratio, which was introduced into the regulatory capital framework in 2014, consistent with international Basel III reforms. The CET1 capital ratio is defined as CET1 capital, which consists primarily of common stock and retained earnings, as a percent of risk-weighted assets. Advanced approaches institutions are required to report risk-weighted assets using an internal model-based approach and a standardized approach. An advanced approaches institution is subject to the lower of the ratios. CBOs that have opted into the community bank leverage ratio (CBLR) framework are not required to report a CET1 capital ratio and risk-weighted assets.

From 2006 through 2013, tier 1 common capital was used to measure common equity capital for all firms. In 2014, both tier 1 common capital (for non-advanced approaches firms) and CET1 capital (for advanced approaches firms) were used. From 2015 to present, CET1 capital has been used for all firms.

**Community Bank Leverage Ratio Framework (CBLR)**

The CBLR framework, which became effective January 1, 2020, allows qualifying CBOs to adopt a simple leverage ratio to measure capital adequacy. To qualify for the framework, a CBO must have less than $10 billion in total consolidated assets, have limited trading activity and off-balance-sheet exposure, meet the leverage ratio requirement, and not be part of an advanced approaches banking organization. The leverage ratio requirement for the CBLR framework was temporarily low-
tered to 8 percent beginning in the second quarter of 2020 through the remainder of calendar year 2020. The requirement was set at 8.5 percent for calendar year 2021 and returned to its previous 9 percent level beginning January 1, 2022.

The leverage ratio requirement for the CBLR framework is defined with respect to tier 1 capital as a percent of average total consolidated assets for the quarter as reported on Schedule RC-K on the Call Report or Schedule HC-K on Form FR Y-9C, as applicable. A CBLR banking organization with a ratio above the requirement will not be subject to other capital and leverage requirements.

**Consumer Loans**

Consumer loans include credit cards, other revolving credit lines, automobile loans, and other consumer loans (including single-payment loans, installment loans excluding automobile loans, and student loans).

**Contingency Funding Plan**

A Contingency Funding Plan (CFP) is a bank’s strategy for addressing contingent liquidity events. Contingent liquidity events are unexpected situations or business conditions that may increase liquidity risk. These events may be institution-specific or arise from external factors. A CFP should contain policies to manage a range of stress environments, establish clear lines of responsibility, and articulate clear implementation and escalation procedures. CFPs should be commensurate with an institution’s complexity, risk profile, and scope of operations. CFPs should address both the severity and duration of contingent liquidity events. CFPs should be regularly tested and updated to ensure that they are operationally sound.

**Credit Default Swap Spread**

The five-year credit default swap spread is the premium payment expressed as a proportion of the notional value of the debt that is being insured against default (typically $10 million in senior debt) in basis points. Data are based on daily polls of individual broker-dealers worldwide. Note that these broker quotes are typically not transaction prices. Data provided are for LISCC firms only.

**Credit Loss Reserves**

Credit loss reserves represent the allowance for credit losses on a bank’s portfolio of financial instruments carried at amortized cost (including loans held for investment, held-to-maturity debt securities, trade receivables, reinsurance receivables, and receivables that relate to repurchase agreements and securities lending agreements), net investment in leases as a lessor, and off-balance-sheet credit exposures not accounted for as insurance or derivatives. Credit loss reserves are recorded on a bank’s balance sheet.
**Delinquent Loans**

Delinquent loans are the sum of 90+ days past due loans and nonaccrual loans.

Note: FR Y-14Q delinquent loans are the sum of 30+ days past due loans and nonaccrual loans.

**Liquid Assets**

Liquid assets are cash plus estimates of securities that qualify as high-quality liquid assets, as defined by the Board’s liquidity coverage ratio rule.

**Market Leverage Ratio**

The market leverage ratio is defined as the ratio of the firm’s market capitalization to the sum of market capitalization and the book value of liabilities. This ratio can be considered a market-based measure of a firm’s capital (expressed in percentage points). Data provided are for LISCC firms only.

**Net Interest Margin**

Net interest margin measures a bank’s yield on its interest-bearing assets after netting out interest expense.

**Prime Brokerage**

Some large banks offer a suite of services to large investment funds known as prime brokerage. These services include the ability to borrow securities or cash, cash management, and access to research as well as provides introductions to potential investors. Lending is an important aspect of these services. The investment funds typically obtain loans secured by equities or other securities through the prime broker.

**Provisions**

Provisions represent the amount necessary to adjust credit loss reserves to reflect management’s current estimate of expected credit losses. Provisions are recorded as an expense item on the bank’s income statement.

**Residential Real Estate Loans**

Residential real estate loans refer to loans secured by 1 to 4 family residential properties, including: revolving, open-end loans secured by 1 to 4 family residential properties and extended under lines of credit; closed-end loans secured by first liens on 1 to 4 family residential properties; and closed-end loans secured by junior (i.e., other than first) liens on 1 to 4 family residential properties.
**Top Holder**

All data, unless otherwise noted, refer to the top-holder data. This population generally comprises top-tier Call Report filers and top-tier FR Y-9C filers, including depository SLHCs and foreign banking organizations. In instances where a top-tier holding company does not file the FR Y-9C, we combine financial data of subsidiary banks/thrifts to approximate the consolidated financial data of the holding company. Commercial and insurance SLHCs, cooperative banks, and non-deposit trust companies are excluded from the top-holder population.

**Tiering of Regulation**

In October 2019, the Federal Reserve Board adopted rules that tier its regulations for domestic and foreign banks and holding companies to match their risk profiles more closely. The rules establish a framework that sorts institutions with $100 billion or more in total assets into four categories based on several factors, including asset size, cross-jurisdictional activity, reliance on weighted short-term wholesale funding (wSTWF), nonbank assets (NBA), and off-balance-sheet exposure (table A.1).
Table A.1. List of domestic and foreign firms, by category, as of 2023:Q4

<table>
<thead>
<tr>
<th>Firm type</th>
<th>Category I U.S. G-SIBs</th>
<th>Category II &gt;=$700b total assets or &gt;=$75b in cross-jurisdictional activity</th>
<th>Category III &gt;=$250b total assets or &gt;=$75b in NBA, wSTWF, or off-balance-sheet exposure</th>
<th>Category IV Other firms with $100b to $250b total assets</th>
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</thead>
<tbody>
<tr>
<td>Domestic firms</td>
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<tr>
<td>U.S. domestic banking organization</td>
<td>Bank of America</td>
<td>Northern Trust</td>
<td>Capital One</td>
<td>Ally Financial</td>
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<td></td>
<td>Bank of New York Mellon</td>
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<td>Charles Schwab</td>
<td>American Express</td>
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<td></td>
<td>Citigroup</td>
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<td>PNC Financial</td>
<td>Citizens Financial</td>
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<td>Goldman Sachs</td>
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<td>Trust Financial</td>
<td>Discover</td>
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<td>JPMorgan Chase</td>
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<td>U.S. Bancorp</td>
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<td>M&amp;T Bank</td>
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<td>NY Community Bancorp</td>
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<td>Regions Financial</td>
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<td>Synchrony Financial</td>
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<tr>
<td>Foreign firms (standards vary by legal entity)</td>
<td>Barclays US</td>
<td>BMO Financial</td>
<td>Credit Suisse USA</td>
<td>HSBC North America</td>
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<td>Deutsche Bank USA</td>
<td>RBC US</td>
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<td>DWS</td>
<td>Santander Holdings USA</td>
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<td>TD Group US</td>
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<td>UBS Americas</td>
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<tr>
<td>Combined U.S. operations</td>
<td>Barclays US</td>
<td>MUFG Sumitomo Mitsui UBS</td>
<td>Bank of Montreal</td>
<td>Banco Santander</td>
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<td>BNP Paribas</td>
<td>Bank of Nova Scotia</td>
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<td>Royal Bank of Canada</td>
<td>Societe Generale</td>
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<td>Toronto-Dominion</td>
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</table>

Notes: NBA is nonbank assets, wSTWF is weighted short-term wholesale funding, BMO Financial moved from Category IV to Category III as of 2023:Q4. Source: FR Y-15.