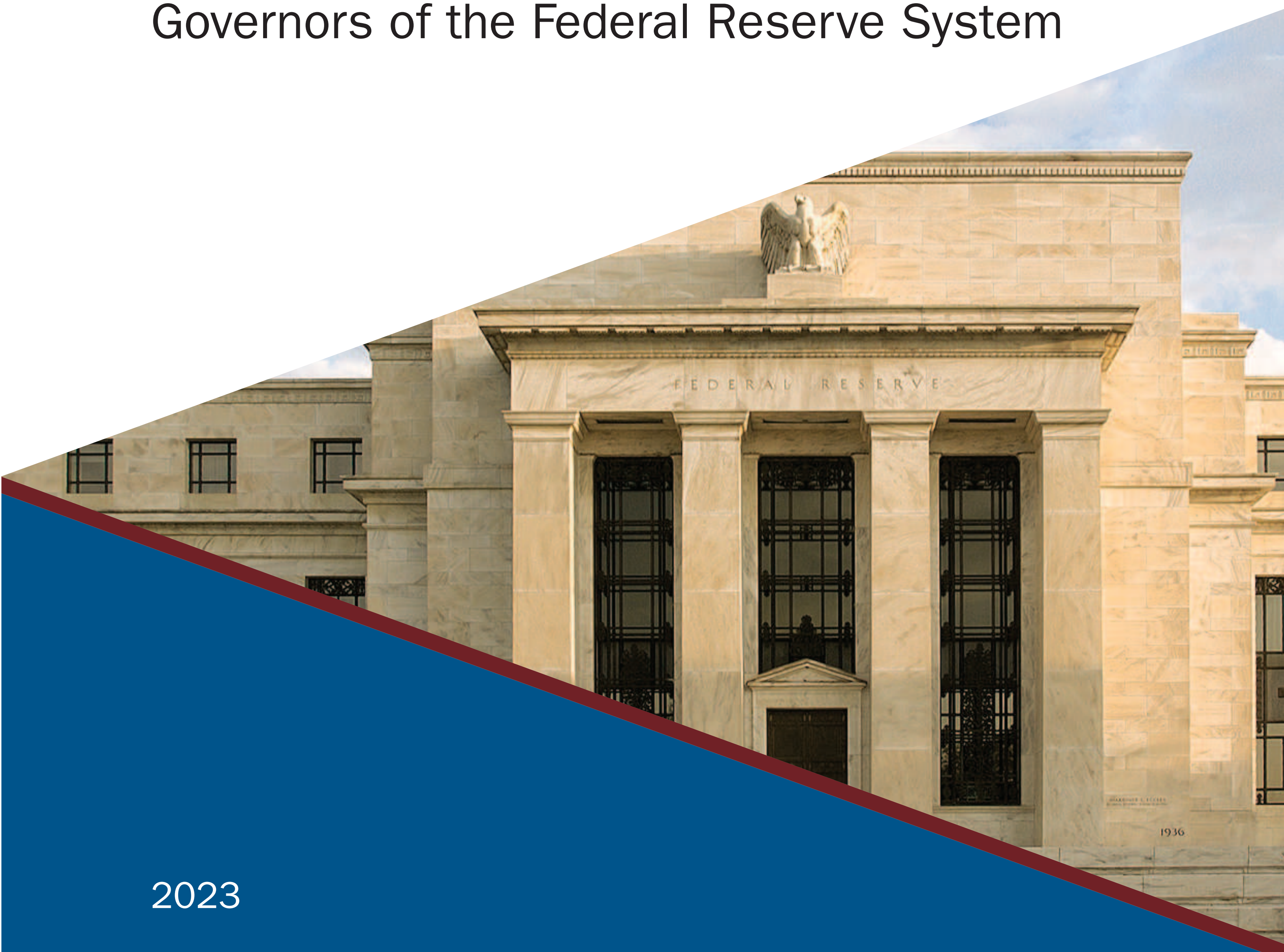
REPORT TO CONGRESS

110th

Annual Report of the Board of Governors of the Federal Reserve System



2023

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Contents

About the Federal Reserve

The Federal Reserve was created by an act of Congress on December 23, 1913, to provide the nation with a safer, more flexible, and more stable monetary and financial system. In establishing the Federal Reserve System, the United States was divided geographically into 12 Districts, each with a separately incorporated Reserve Bank.

For more information about the Federal Reserve Board and the Federal Reserve System, visit the Board's website at https://www.federalreserve.gov/aboutthefed/default.htm. Online versions of the Board's annual report are available at https://www.federalreserve.gov/publications/annual-report/default.htm.

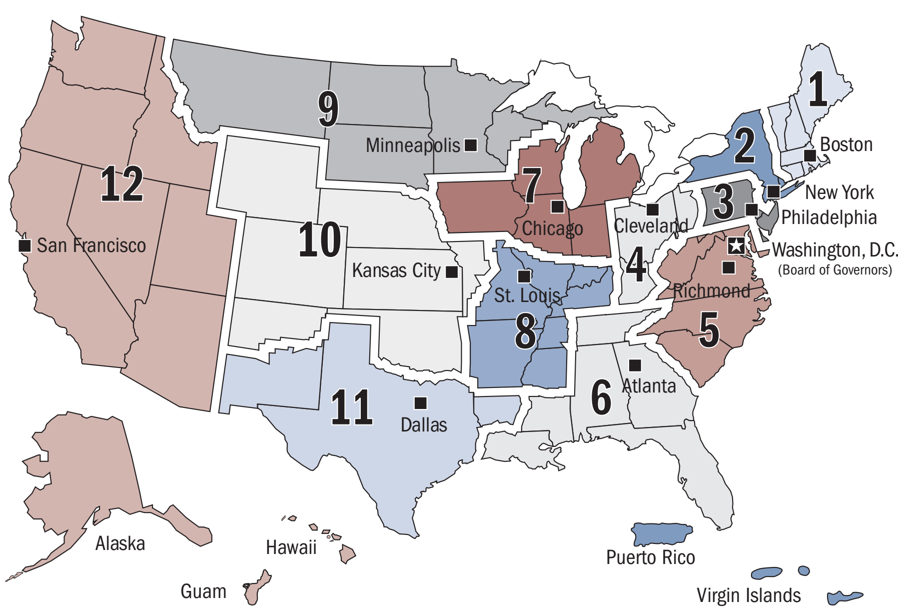
1 | Overview

This report covers the calendar-year 2023 operations and activities of the Federal Reserve, the central bank of the United States (see figure 1.1), categorized in the five key functional areas:

- **Conducting monetary policy and monitoring economic developments.** Section 2 provides adapted versions of the Board's semiannual Monetary Policy Reports to Congress.
- **Promoting financial system stability.** Section 3 reviews Board and System activities and research undertaken to foster a resilient and stable financial system.
- **Supervising and regulating financial institutions and their activities.** Section 4 summarizes the Board's efforts related to financial institution oversight and examinations, supervisory policymaking, and regulatory activities and enforcement.
- **Fostering payment and settlement system safety and efficiency.** Section 5 describes actions by the Board and Reserve Banks to promote the effectiveness of the nation's payment systems, discusses initiatives to promote payment system safety, and provides data on Reserve Bank services and income.
- **Promoting consumer protection and community development.** Section 6 provides information on the Board's efforts to promote a fair and transparent financial services market for con-

Figure 1.1. The Federal Reserve System's unique structure ensures broad perspective

The Federal Reserve System consists of 12 Reserve Banks located in major cities throughout the United States, along with a seven-member Board of Governors headquartered in Washington, D.C. See "Federal Reserve System Organization" in appendix A for more information on the Board and System leadership.



sumers, protect consumer rights, and ensure that Board policies and research take consumer and community perspectives into account.

Additional information for calendar-year 2023 on Federal Reserve leadership, policy actions, budgets as well as historical data and supporting activities can be found in the appendixes:

- Appendix A lists key officials across the Federal Reserve System
- Appendix B provides links to the minutes for each of the eight regularly scheduled meetings of the Federal Open Market Committee
- Appendix C contains information on the Federal Reserve's audited financial statements as well as reviews conducted by the Office of Inspector General and the Government Accountability Office
- Appendix D presents information on the budgets for the Board and Reserve Banks and on currency-related costs
- Appendix E summarizes policy actions of the Board of Governors
- Appendix F lists litigation, both pending and resolved, that the Board of Governors was a party in
- Appendix G includes statistical tables that provide updated historical data concerning Board and System operations and activities

2 | Monetary Policy and Economic Developments

The Federal Reserve conducts the nation's monetary policy to promote maximum employment, stable prices, and moderate long-term interest rates in the U.S. economy. This section reviews U.S. monetary policy and economic developments in 2023 by providing excerpts and select figures from the *Monetary Policy Report* published in March 2024 and June 2023.[1] The report, submitted semiannually to the Congress, is delivered concurrently with testimony from the Federal Reserve Board Chair.[2]

March 2024 Summary

While inflation remains above the Federal Open Market Committee's (FOMC) objective of 2 percent, it has eased substantially over the past year, and the slowing in inflation has occurred without a significant increase in unemployment. The labor market remains relatively tight, with the unemployment rate near historically low levels and job vacancies still elevated. Real gross domestic product (GDP) growth has also been strong, supported by solid increases in consumer spending.

The FOMC has maintained the target range for the federal funds rate at 5¼ to 5½ percent since its July 2023 meeting. The Committee views the policy rate as likely at its peak for this tightening cycle, which began in early 2022. The Federal Reserve has also continued to reduce its holdings of Treasury and agency mortgage-backed securities.

As labor market tightness has eased and progress on inflation has continued, the risks to achieving the Committee's employment and inflation goals have been moving into better balance. Even so, the Committee remains highly attentive to inflation risks and is acutely aware that high inflation imposes significant hardship, especially on those least able to meet the higher costs of essentials.

The FOMC is strongly committed to returning inflation to its 2 percent objective. In considering any adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. The Committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent.

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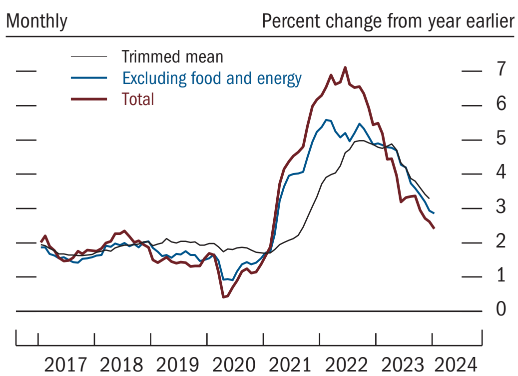
[1] Those complete reports are available on the Board's website at https://www.federalreserve.gov/publications/files/20240301_mprfullreport.pdf (March 2024) and https://www.federalreserve.gov/monetarypolicy/files/20230616_mprfullreport.pdf (June 2023).

[2] As required by section 2B of the Federal Reserve Act, the Federal Reserve Board submits written reports to the Congress that contain discussions of "the conduct of monetary policy and economic developments and prospects for the future."

Recent Economic and Financial Developments

Inflation. Consumer price inflation has slowed notably but remains above 2 percent. The price index for personal consumption expenditures (PCE) rose 2.4 percent over the 12 months ending in January, down from a peak of 7.1 percent in 2022. The core PCE price index—which excludes volatile food and energy prices and is generally considered a better guide to the direction of future inflation—rose 2.8 percent in the 12 months ending in January, and the slowing in inflation was widespread across both goods and services prices (figure 2.1). More recently, core PCE prices increased at an annual rate of 2.5 percent over the six months ending in January, though measuring inflation over relatively short periods risks exaggerating the influence of idiosyncratic or temporary factors. Measures of longer-term inflation expectations are within the range of values seen in the decade before the pandemic and continue to be broadly consistent with the FOMC's longer-run objective of 2 percent.

Figure 2.1. Personal consumption expenditures price indexes

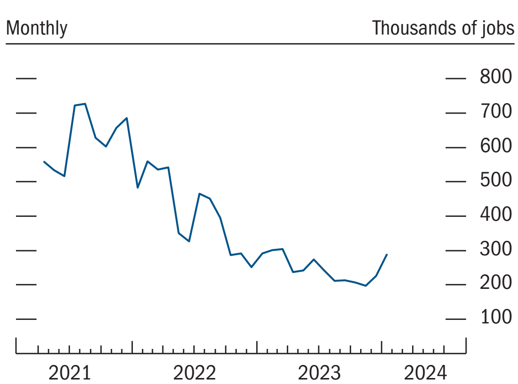


Note: Trimmed mean data extend through December 2023. All other data extend through January 2024.

Source: For trimmed mean, Federal Reserve Bank of Dallas; for all else, Bureau of Economic Analysis; all via Haver Analytics.

The labor market. The labor market has remained relatively tight, with job gains averaging 239,000 per month since June and the unemployment rate near historical lows (figure 2.2). Labor demand has eased—as job openings have declined in many sectors of the economy—but continues to exceed the supply of available workers (figure 2.3). Labor supply has trended higher over the past year, reflecting a continued strong pace of immigration and increases in the labor force participation rate, particularly among prime-age workers. Reflecting the improved balance between labor demand and supply, nominal wage gains slowed in 2023, but they remain above a pace consistent with 2 percent inflation over the longer term, given prevailing trends in productivity growth.

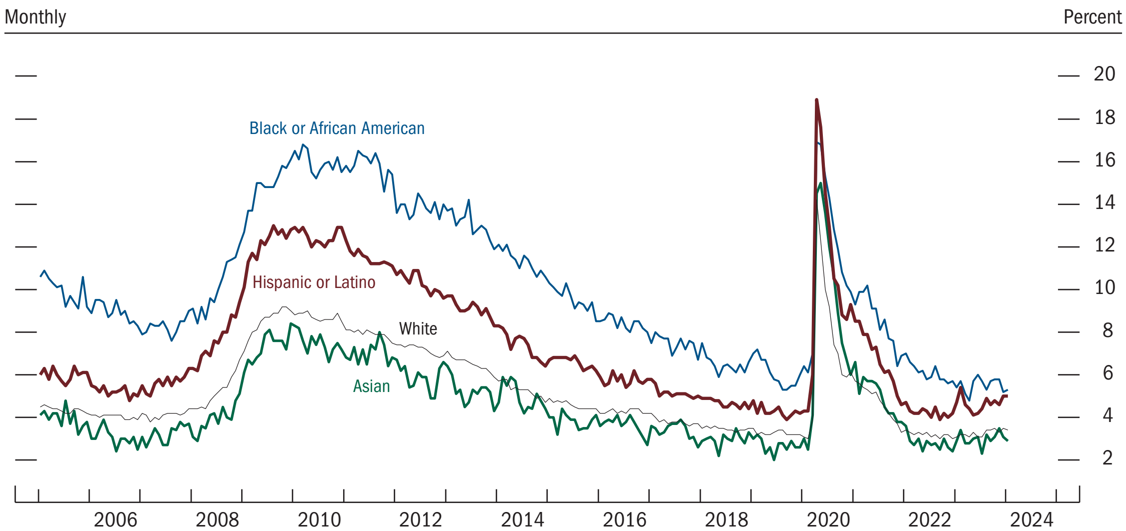
Figure 2.2. Nonfarm payroll employment



Note: The data shown are a 3-month moving average of the change in nonfarm payroll employment and extend through January 2024.

Source: Bureau of Labor Statistics via Haver Analytics.

Figure 2.3. Unemployment rate, by race and ethnicity



Note: Unemployment rate measures total unemployed as a percentage of the labor force. Persons whose ethnicity is identified as Hispanic or Latino may be of any race. Small sample sizes preclude reliable estimates for Native Americans and other groups for which monthly data are not reported by the Bureau of Labor Statistics. The data extend through January 2024.

Source: Bureau of Labor Statistics via Haver Analytics.

Economic activity. Real GDP increased 3.1 percent last year, notably faster than in 2022 despite tighter financial conditions, including elevated longer-term interest rates. Consumer spending grew at a solid pace, and housing market activity started to turn back up in the second half of last year after having declined since early 2021. However, real business fixed investment growth slowed, likely reflecting tighter financial conditions and downbeat business sentiment. In contrast to GDP, manufacturing output was little changed, on net, last year, a downshift following two years of robust post-pandemic gains.

Financial conditions. Conditions in financial markets tightened considerably further over the summer and early fall before reversing course toward the end of the year. The FOMC raised the target range for the federal funds rate a further 25 basis points at its meeting last July, bringing the overall increase in the target range for this tightening cycle to 525 basis points. The market-implied expected path of the federal funds rate has moved up, on net, since the middle of 2023, and yields on longer-term nominal Treasury securities are notably higher on balance. Credit remains generally available to most households and businesses but at elevated interest rates, which have weighed on financing activity. Lending by banks to households and businesses slowed notably since June as banks continued to tighten standards and demand for loans softened.

Financial stability. Overall, the banking system remains sound and resilient; although acute stress in the banking system has receded since last March, a few areas of risk warrant continued monitoring. Upward pressure on asset valuations continued, with real estate prices elevated relative to rents and high price-to-earnings ratios in equity markets. Borrowing from nonfinancial businesses and households continued to increase at a pace slower than that of nominal GDP, and the combined debt-to-GDP ratio now sits close to its 20-year low. Vulnerabilities from financial-sector leverage remain notable. While risk-based bank capital ratios stayed solid and increased broadly, declines in the fair values of fixed-rate assets have been sizable relative to the regulatory capital at some banks. Meanwhile, leverage at hedge funds has stabilized at high levels, and leverage at life insurers increased to values close to the historical averages but with a liability composition that has become more reliant on nontraditional sources of funding. Most banks maintained high liquidity and stable funding, while bank funding costs continue to increase. (See the box "Developments Related to Financial Stability" on pages 27–28 of the March 2024 *Monetary Policy Report*.)

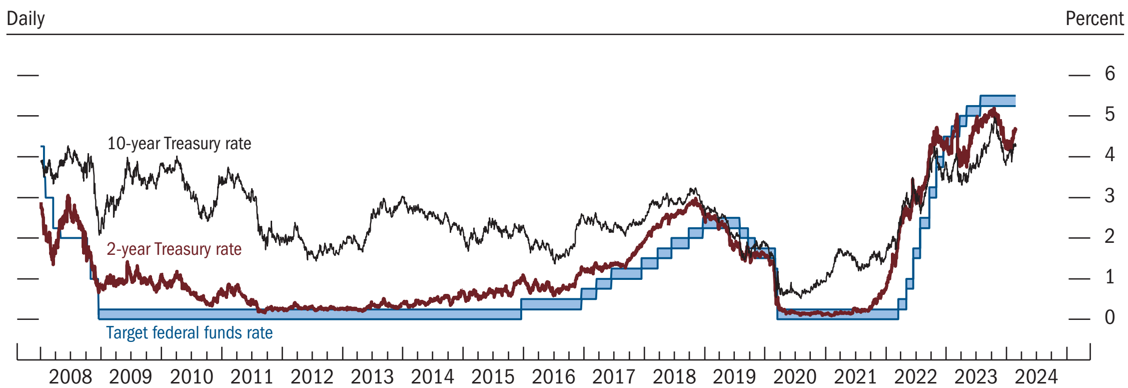
International developments. Following a rebound in early 2023, growth in foreign economic activity was subdued in the second half of last year. Economic growth was particularly weak in advanced foreign economies (AFEs) as monetary policy tightening weighed on activity and high inflation eroded real household incomes. Structural adjustment to higher energy prices in Europe continued to hinder economic performance, while property-sector weakness and sluggish domestic demand restrained Chinese economic activity. Foreign headline inflation has fallen further, reflecting declines in core and food inflation. However, the pace of disinflation has varied across countries and sectors, with the moderation in goods inflation generally outpacing that in services inflation.

Most foreign central banks paused policy interest rate hikes in the second half of last year and have since held rates steady. Policy rate paths implied by financial market pricing suggest that central banks in many AFEs are expected to begin lowering their policy rates in 2024. Several central banks in emerging market economies have already begun easing monetary policy. The trade-weighted exchange value of the U.S. dollar has increased slightly, on net, since the middle of last year.

Monetary Policy

Interest rate policy. After significantly tightening the stance of monetary policy since early 2022, the FOMC has maintained the target range for the policy rate at 5¼ to 5½ percent since its meeting last July (figure 2.4). Although the FOMC judges that the risks to achieving its employment and inflation goals are moving into better balance, the Committee remains highly attentive to inflation risks. The Committee has indicated that it does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward

Figure 2.4. Selected interest rates



Note: The 2-year and 10-year Treasury rates are the constant-maturity yields based on the most actively traded securities. The data extend through February 27, 2024.

Source: Department of the Treasury; Federal Reserve Board.

2 percent. In considering any adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks.

Balance sheet policy. The Federal Reserve has continued the process of significantly reducing its holdings of Treasury and agency securities in a predictable manner, contributing to the tightening of financial conditions.[3] Beginning in June 2022, principal payments from securities held in the System Open Market Account have been reinvested only to the extent that they exceeded monthly caps. Under this policy, the Federal Reserve has reduced its securities holdings about $640 billion since mid-June 2023, bringing the total reduction in securities holdings since the start of balance sheet runoff to about $1.4 trillion. The FOMC has stated that it intends to maintain securities holdings at amounts consistent with implementing monetary policy efficiently and effectively in its ample-reserves regime. To ensure a smooth transition, the FOMC intends to slow and then stop reductions in its securities holdings when reserve balances are somewhat above the level that the FOMC judges to be consistent with ample reserves.

Special Topics

Employment and earnings across groups. An exceptionally tight labor market over the past two years has been especially beneficial for historically disadvantaged groups of workers. As a result, many of the long-standing disparities in employment and wages by sex, race, ethnicity, and education have narrowed, and some gaps reached historical lows in 2023. However, despite this nar-

[3] See the May 4, 2022, press release regarding the Plans for Reducing the Size of the Federal Reserve's Balance Sheet, available on the Board's website at https://www.federalreserve.gov/newsevents/pressreleases/monetary20220504b.htm.

rowing, significant disparities in absolute levels across groups remain. (See the box "Employment and Earnings across Demographic Groups" on pages 10–12 of the March 2024 *Monetary Policy Report*.)

Housing sector. The rise in mortgage rates over the past two years has reduced housing demand, resulting in a steep drop in housing activity in 2022 and a marked slowing in house price growth from its historically high pace. Offsetting factors boosting housing demand, such as the robust job market and the increased prevalence of remote work, have prevented significant price declines. High mortgage rates have also discouraged some potential sellers with low rates on their current mortgages from moving, which has kept the existing home market unusually thin. The shortage of available existing homes has pushed some remaining homebuyers toward new homes and supported a modest rebound in construction of single-family homes later in 2023. In contrast, multifamily starts rose to historically high levels in 2022 but have more recently fallen back because of builders' concerns about the effect of the significant amount of new multifamily supply on rents and property prices. (See the box "Recent Housing Market Developments" on pages 19–21 of the March 2024 *Monetary Policy Report*.)

Federal Reserve's balance sheet and money markets. The size of the Federal Reserve's balance sheet has decreased since June as the FOMC continued to reduce its securities holdings. Despite ongoing balance sheet runoff, reserve balances—the largest liability on the Federal Reserve's balance sheet—edged up as declines in the usage of the overnight reverse repurchase agreement facility—another Federal Reserve liability—more than matched the decline in assets. (See the box "Developments in the Federal Reserve's Balance Sheet and Money Markets" on pages 38–40 of the March 2024 *Monetary Policy Report*.)

Monetary policy rules. Simple monetary policy rules, which prescribe a setting for the policy interest rate in response to the behavior of a small number of economic variables, can provide useful guidance to policymakers. With inflation easing and supply and demand conditions in labor markets coming into better balance, the policy rate prescriptions of most simple monetary policy rules have decreased recently and now call for levels of the federal funds rate that are close to the current target range for the federal funds rate. (See the box "Monetary Policy Rules in the Current Environment" on pages 41–43 of the March 2024 *Monetary Policy Report*.)

June 2023 Summary

Although inflation has moderated somewhat since the middle of last year, it remains well above the Federal Open Market Committee's (FOMC) objective of 2 percent. The labor market continues to be very tight, with robust job gains and the unemployment rate near historically low levels, though nominal wage growth has shown some signs of easing and job vacancies have declined. Real gross domestic product (GDP) growth was modest in the first quarter, despite a pickup in consumer spending. Bringing inflation back to 2 percent will likely require a period of below-trend growth and some softening of labor market conditions.

In response to high inflation, the FOMC continued to increase interest rates and reduce its securities holdings. The FOMC has raised the target range for the federal funds rate a further 75 basis points since the start of the year, bringing the range to 5 to 5¼ percent. In determining the extent of additional policy firming that may be appropriate to return inflation to 2 percent over time, the FOMC indicated that it will take into account the cumulative tightening of monetary policy, the lags with which monetary policy affects economic activity and inflation, and economic and financial developments. The Federal Reserve also continued to reduce its holdings of Treasury and agency mortgage-backed securities; these holdings have declined by about $420 billion since January, further tightening financial conditions.

The Federal Reserve is acutely aware that high inflation imposes significant hardship, especially on those least able to meet the higher costs of essentials. The FOMC is strongly committed to returning inflation to its 2 percent objective.

Recent Economic and Financial Developments

Inflation. Consumer price inflation, as measured by the 12-month change in the price index for personal consumption expenditures (PCE), was 4.4 percent in April, down from its peak of 7.0 percent last June but still well above the FOMC's 2 percent objective. Core PCE price inflation—which excludes volatile food and energy prices and is generally considered a better guide to the direction of future inflation—is also off its peak but was still 4.7 percent over the 12 months ending in April. As supply chain bottlenecks have eased and demand has stabilized, increases in core goods prices slowed considerably over the past year. Within core services prices, housing services inflation has been high, but the monthly changes have started to ease in recent months, consistent with the slower increases in rents for new tenants that have been observed since the second half of last year. For other core services, price inflation remains elevated and has not shown signs of easing, and prospects for slowing inflation may depend in part on a further easing of tight labor market conditions. Measures of longer-term inflation expectations are within the range of values seen in the decade before the pandemic and continue to be broadly consistent with the FOMC's longer-run objective of 2 percent, suggesting that high inflation is not becoming entrenched.

The labor market. The labor market has remained very tight, with job gains averaging 314,000 per month during the first five months of the year and the unemployment rate remaining near historical lows. Labor demand has eased in many sectors of the economy but continues to exceed the supply of available workers, with job vacancies still elevated. Labor supply has improved, with a pickup in immigration and an improvement in the labor force participation rate, particularly among prime-age workers. Nominal wage gains continued to slow in the first half of 2023, but they remain above the pace consistent with 2 percent inflation over the longer term, given prevailing trends in productivity growth.

Economic activity. After the strong rebound in 2021 from the pandemic-induced recession, economic activity lost momentum last year, and growth in the first quarter of this year was modest as financial conditions continued to tighten. Real consumer spending grew at a solid pace in the first quarter but appears to be moderating as consumer financing conditions have tightened and consumer confidence has remained low. Real business fixed investment growth continued to slow in the first quarter, likely reflecting tighter financial conditions and weaker output growth, while manufacturing output has been roughly unchanged so far this year after having declined in the fourth quarter. Activity in the housing sector continued to contract in response to elevated mortgage rates, but several indicators appear to have bottomed out.

Financial conditions. Financial conditions have tightened further since January. The FOMC has raised the target range for the federal funds rate a further 75 basis points since January, and the market-implied expected path of the federal funds rate over the next year shifted up. Though yields on longer-term nominal Treasury securities were little changed, on net, over this period, the relatively high level of interest rates has weighed on financing activity. Business loans at banks grew since the start of 2023, but the pace of growth continued to slow as banks tightened standards and average borrowing costs rose. Investment-grade corporate bond issuance rebounded to a brisk pace in May, following a slowdown in March and April. Speculative-grade issuance rebounded as well but was still subdued by historical standards. While business credit quality remains strong, some indicators of future business defaults are somewhat elevated. For households, mortgage originations remained weak, although consumer loans (such as auto loans and credit cards) grew further. After having risen last year, delinquency rates leveled off in the first quarter for auto loans and continued to increase for credit card loans.

Financial stability. Despite concerns about profitability at some banks, the banking system remains sound and resilient. Most measures of valuation pressures in corporate securities markets remained near the middle of their historical distributions. By contrast, valuation pressures in commercial and residential real estate markets continued to be elevated. Borrowing by households and businesses grew a bit more slowly than GDP, leaving vulnerabilities arising from household and business debt largely unchanged at moderate levels. In the banking sector, heavy reliance on uninsured deposits, declining fair values of long-duration fixed-rate assets associated with higher interest rates, and poor risk management led to the failure of three domestic banks. Broad bank equity prices fell sharply as market participants reassessed the strength of some banks with similar risk profiles to those that failed. However, the broader banking sector maintained substantial loss-absorbing capacity and ample liquidity. In the nonbank financial sector, leverage at hedge funds remained elevated, and structural vulnerabilities associated with funding risk persisted at some money market funds and certain mutual funds. (See the box "Developments Related to Financial Stability" on pages 31–32 of the June 2023 *Monetary Policy Report*.)

International developments. Following a slowdown at the end of 2022, foreign activity rebounded early this year. This rebound was driven in part by strong growth in China, as the lifting of COVID-19 restrictions unleashed pent-up demand, though recent indicators suggest that momentum is slowing. Europe showed resilience to the energy price shock stemming from Russia's war against Ukraine. Foreign headline inflation continued to fall, driven by declines in retail energy prices. However, while energy inflation has moderated in many foreign economies, both food and core inflation remain elevated.

Since January, several major foreign central banks continued tightening their monetary policies, communicating concerns about elevated inflation and tight labor markets. That said, some central banks also emphasized the need to be cautious in their approach, given the lags of monetary policy and the uncertainty about the outlook for growth and inflation. The trade-weighted exchange value of the U.S. dollar is a touch lower.

Monetary Policy

In response to high inflation, the FOMC continued to increase the target range for the federal funds rate and reduce its securities holdings this year. Adjustments to both interest rates and the balance sheet are playing a role in firming the stance of monetary policy in support of the Federal Reserve's maximum-employment and price-stability goals.

Interest rate policy. The FOMC continued to increase the target range for the federal funds rate, bringing it to the current range of 5 to 5¼ percent. In light of the cumulative tightening of monetary policy and the lags with which monetary policy affects economic activity and inflation, the FOMC slowed the pace of policy tightening relative to last year. The FOMC will determine meeting by meeting the extent of additional policy firming that may be appropriate to return inflation to 2 percent over time, based on the totality of incoming data and their implications for the outlook for economic activity and inflation.

Balance sheet policy. The Federal Reserve has continued the process of significantly reducing its holdings of Treasury and agency securities in a predictable manner.[4] Beginning in June of last year, principal payments from securities held in the System Open Market Account (SOMA) have been reinvested only to the extent that they exceeded monthly caps. The Federal Reserve has reduced its securities holdings by about $420 billion since January. This decrease in assets was partially offset by liquidity provisions to the banking system following the banking-sector stresses in March.

Special Topics

Employment and earnings across groups. Strong labor demand over the past two years has particularly benefited historically more disadvantaged workers. As a result, many of the disparities in employment and wages across racial, ethnic, sex, and education groups, which had been exacerbated by the pandemic, have narrowed—in some cases to historically narrow ranges. Despite this narrowing, there remain significant disparities in absolute levels of employment and wages across groups. (See the box "Developments in Employment and Earnings across Demographic Groups" on pages 11–13 of the June 2023 *Monetary Policy Report*.)

Bank stress and lending. Bank lending conditions have tightened notably over the past year, and bank loan growth has slowed, following the tightening of monetary policy that started in early 2022. Banking-sector strains in March 2023 reportedly led to further tightening in lending conditions at some banks. Results from the April 2023 Senior Loan Officer Opinion Survey on Bank Lending Practices show that banks expect to further tighten their lending standards over the remainder of 2023, with some banks reporting concerns about their liquidity positions, deposit outflows, and funding costs. Economic research suggests that tighter credit conditions at banks can have adverse effects on economic activity, but different studies find effects that vary in scope, magnitude, and timing. In terms of scope, the effects are also likely to differ across borrowers, economic sectors, and geographic areas, and they may be larger for sectors that depend more heavily on bank credit, such as the commercial real estate and the small business sectors. (See the box "Recent Developments in Bank Lending Conditions" on pages 21–23 of the June 2023 *Monetary Policy Report*.)

Federal Reserve's balance sheet and money markets. The Federal Reserve continued to reduce the size of its SOMA portfolio. However, in March, amid banking-sector developments, borrowing from the discount window increased, and the Federal Reserve implemented a new facility, the Bank Term Funding Program (BTFP), to make additional funding available to eligible depository institutions. As a result of Federal Reserve lending through the BTFP, the discount window, and other credit extensions, the Federal Reserve's total assets have increased since March. Take-up

[4] See the May 4, 2022, press release regarding the Plans for Reducing the Size of the Federal Reserve's Balance Sheet, available on the Board's website at https://www.federalreserve.gov/newsevents/pressreleases/monetary20220504b.htm.

in the overnight reverse repurchase agreement (ON RRP) facility remained elevated, as low rates on repurchase agreements persisted amid still abundant liquidity and limited Treasury bill supply. The ON RRP facility continued to serve its intended purpose of helping to provide a floor under short-term interest rates and supporting effective implementation of monetary policy. (See the box "Developments in the Federal Reserve's Balance Sheet and Money Markets" on pages 42–43 of the June 2023 *Monetary Policy Report*.)

Monetary policy rules. Simple monetary policy rules, which prescribe a setting for the policy interest rate based on a small number of other economic variables, can provide useful guidance to policymakers. Since 2021, inflation has run well above the FOMC's 2 percent longer-run objective, and labor market conditions have been very tight over the past year. As a result, simple monetary policy rules have called for elevated levels of the federal funds rate. (See the box "Monetary Policy Rules in the Current Environment" on pages 44–46 of the June 2023 *Monetary Policy Report*.)

3 | Financial Stability

The Federal Reserve monitors financial system risks and engages at home and abroad to help ensure that the system supports a healthy economy for U.S. households, communities, and businesses.

In order to maintain a resilient financial system, the Federal Reserve monitors the potential buildup of risks to financial stability; uses such analyses to inform Federal Reserve responses, including the design of stress-test scenarios and decisions regarding other policy tools, such as the countercyclical capital buffer; works with other domestic agencies directly and through the Financial Stability Oversight Council (FSOC); and engages with the global community in monitoring, supervision, and regulation efforts that mitigate the risks and consequences of financial instability domestically and abroad.[1]

This section discusses key financial stability activities undertaken by the Federal Reserve over 2023, which include the following:

1. monitoring vulnerabilities that affect financial stability (see figure 3.1 for a summary of key vulnerabilities);
2. promoting a perspective on the supervision and regulation of large, complex financial institutions that accounts for the potential spillovers from distress at such institutions to the financial system and broader economy; and
3. engaging in domestic and international cooperation and coordination.

Periodically, Federal Reserve Board staff assess potential vulnerabilities relevant for financial system stability. These monitoring efforts promote financial stability by informing broader policy discussions and stimulating additional research.

Some of these activities are also discussed elsewhere in this annual report. A broader set of economic and financial developments are discussed in section 2, "Monetary Policy and Economic Developments," with the discussion that follows concerning surveillance of economic and financial developments focused on financial stability. The full range of activities associated with supervision of systemically important financial institutions and designated financial market utilities is discussed in section 4, "Supervision and Regulation."

[1] For more information on how the Federal Reserve promotes a stable financial system, see the section "Promoting Financial System Stability" in *The Fed Explained: What the Central Bank Does,* available on the Board's website at https://www.federalreserve.gov/aboutthefed/files/the-fed-explained.pdf#page=50.

Figure 3.1. The Federal Reserve assesses four key vulnerabilities in monitoring financial stability

Each quarter, Federal Reserve Board staff assess a set of four vulnerabilities relevant for financial system stability. These monitoring efforts promote financial stability by informing broader policy discussions and stimulating additional research.

Asset valuations	Borrowing by businesses and households	Leverage in the financial sector	Funding risk
Why it matters:	**Why it matters:**	**Why it matters:**	**Why it matters:**
Overvalued assets are a vulnerability because the unwinding of high prices can be destabilizing.	Excessive borrowing by businesses and households leaves them vulnerable to distress if their incomes decline or the assets they own fall in value.	Excessive leverage within the financial sector increases the risk that financial institutions will not have the ability to absorb even modest losses when hit by adverse shocks.	Funding risks expose the financial system to the possibility that investors will “run” by quickly withdrawing their funds from a particular institution or sector.

Monitoring Financial Vulnerabilities

This section describes the Federal Reserve’s monitoring of vulnerabilities in the financial system during 2023.

Financial institutions are linked together through a complex set of relationships, and their resilience depends on the economic condition of households and businesses. In turn, the condition of households and businesses hinges on the strength of financial institutions’ balance sheets, as the nonfinancial sector obtains funding through the financial sector. The Federal Reserve’s measures to monitor risks to financial stability are designed to better understand these complex linkages and have been an important part of the Federal Reserve’s efforts to achieve overall economic stability.

A stable financial system, when hit by adverse events, or “shocks,” is able to continue meeting demands for financial services from households and businesses, such as credit provision and payment services. By contrast, in an unstable system, these same shocks are likely to have much larger effects, disrupting the flow of credit and leading to declines in employment and economic activity.

Consistent with this view of financial stability, the Federal Reserve Board's monitoring framework distinguishes between shocks to and vulnerabilities of the financial system. Shocks, such as sudden changes to financial or economic conditions, are inherently hard to predict. Vulnerabilities tend to build up over time and are the aspects of the financial system that are most expected to cause widespread problems in times of stress.

Accordingly, the Federal Reserve maintains a flexible, forward-looking financial stability monitoring program focused on assessing how the level and configuration of those vulnerabilities affect the financial system's resilience to a wide range of potential adverse shocks.

Each quarter, Federal Reserve Board staff assess a set of vulnerabilities relevant for financial stability, including, but not limited to, asset valuation pressures, borrowing by households and businesses, leverage in the financial sector, and funding risk. These monitoring efforts inform discussions concerning policies to promote financial stability, such as supervision and regulatory policies as well as monetary policy. They also inform Federal Reserve interactions with broader monitoring efforts, such as those by the FSOC and the Financial Stability Board (FSB).

Since 2018, the Federal Reserve Board has also published its *Financial Stability Report,* which summarizes the Board's framework for assessing the resilience of the U.S. financial system and presents the Board's current assessment of financial system vulnerabilities.[2] It aims to promote public understanding about Federal Reserve views on this topic and thereby increase transparency and accountability. The report complements the annual report of the FSOC, which is chaired by the Secretary of the Treasury and includes the Federal Reserve Chair and other financial regulators.

Asset Valuation Pressures

Overvalued assets are a vulnerability because the unwinding of high prices can be destabilizing, especially if the assets are widely held and the values are supported by excessive leverage, maturity transformation, or risk opacity. Moreover, stretched asset valuations may be an indicator of a broader buildup in risk-taking. Because it is very difficult to judge whether an asset price is overvalued relative to fundamentals, the Federal Reserve's analysis of asset valuation pressures typically tracks a broad range of measures, including price volatility, underwriting standards, and investor flows.

The economy remained strong over the year, and the economic outlook centered on continued growth. Against this backdrop, valuation pressures across different sectors remained notable.

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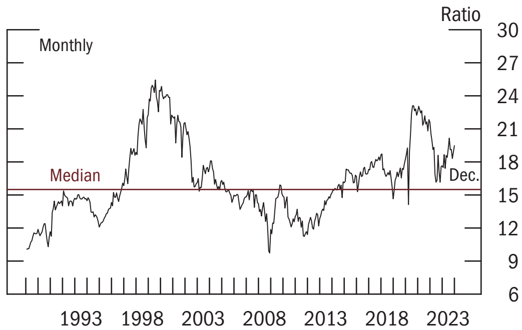
[2] See Board of Governors of the Federal Reserve System, *Financial Stability Report* (Washington: Board of Governors, April 2024), https://www.federalreserve.gov/publications/files/financial-stability-report-20240419.pdf; and Board of Governors of the Federal Reserve System, *Financial Stability Report* (Washington: Board of Governors, October 2023), https://www.federalreserve.gov/publications/files/financial-stability-report-20231020.pdf.

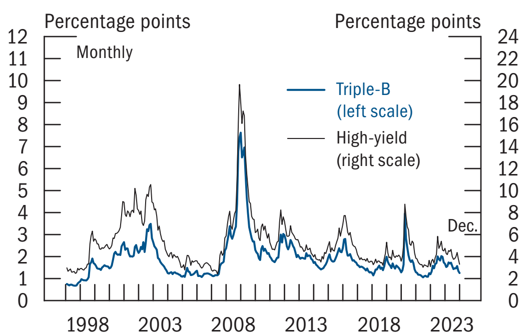
Figure 3.2. Aggregate forward price-to-earnings ratio of S&P 500 firms, 1989–2023



Note: Based on expected earnings for 12 months ahead. The median value is 15.6.

Source: Federal Reserve Board staff calculations using Refinitiv, Institutional Brokers' Estimate System estimates.

Figure 3.3. Corporate bond spreads to similar-maturity Treasury securities, 1997–2023



Note: The triple-B series reflects the option-adjusted spread of the ICE Bank of America Merrill Lynch (BofAML) triple-B U.S. Corporate Index (C0A4), and the high-yield series reflects the option-adjusted spread of the ICE BofAML U.S. High Yield Index (H0A0).

Source: ICE Data Indices, LLC, used with permission.

Equity prices were still high relative to earnings (figure 3.2). In addition, real estate prices continued to be high relative to fundamentals. Spreads on corporate bonds and loans ended 2023 at levels below those seen over most of 2022 and 2023 and similar to the levels seen in the late 2010s (figure 3.3).

Valuation pressures in the residential real estate sector remained elevated by historical standards. Despite high borrowing costs and tightening of lending standards, various house price indexes showed increases over the year. The price-to-rent ratio remained at the upper end of its historical distribution, supported by a tight inventory of homes for sale.

Commercial real estate (CRE) prices remained high relative to fundamentals despite the continued decline in prices in most segments. Amid low transaction volumes, transaction-based prices may not fully reflect the deterioration in CRE markets, because rather than realizing losses, owners could decide not to put their properties on the market and instead choose to wait for more favorable conditions. Finally, farmland prices continued to increase, supported by high commodity prices and limited farmland inventories.

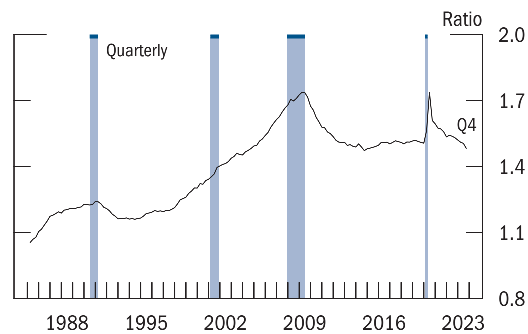
Borrowing by Households and Businesses

Excessive borrowing by households and businesses has been an important contributor to past financial crises. When highly indebted households and nonfinancial businesses are hit by negative shocks to incomes or asset values, they may be forced to curtail spending, which could then amplify the effects of financial shocks.

In turn, financial stress among households and businesses can lead to mounting losses at financial institutions, creating an adverse feedback loop in which weaknesses among households, nonfinancial businesses, and financial institutions cause further declines in income and accelerate financial losses, potentially leading to financial instability and a sharp contraction in economic activity.

A commonly used measure of the financial position of households and businesses is the ratio of the combined total debt of nonfinancial businesses and households relative to gross domestic product (GDP). Total debt declined over the year, even as nominal GDP continued to grow in 2023, leaving the credit-to-GDP ratio close to its lowest level in 20 years (figure 3.4). This development suggests that, in the aggregate, households and businesses do not appear to have borrowed excessively.

Figure 3.4. Private nonfinancial-sector credit-to-GDP ratio, 1985–2023



Note: The shaded bars with top caps indicate periods of business recession as defined by the National Bureau of Economic Research: July 1990 to March 1991, March 2001 to November 2001, December 2007 to June 2009, and February 2020 to April 2020. GDP is gross domestic product.

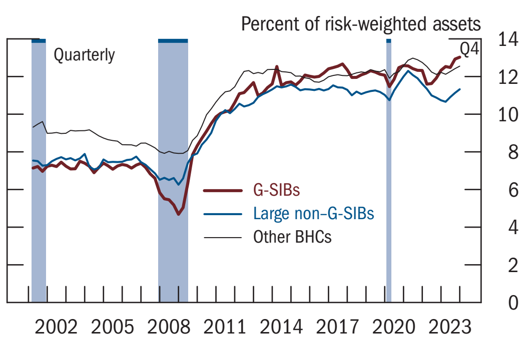
Source: Federal Reserve Board staff calculations based on Bureau of Economic Analysis, national income and product accounts, and Federal Reserve Board, Statistical Release Z.1, "Financial Accounts of the United States."

Separate examination of business and household borrowing yields some additional insights. The gross leverage of large businesses—the ratio of debt to assets for all publicly traded nonfinancial firms—declined slightly but remained elevated by historical standards. Net leverage—the ratio of debt less cash to assets—showed a similar trend. The ability of public firms to service their debt, as measured by the interest coverage ratio, remained high by historical standards, in part reflecting solid earnings. The adverse effect of rising interest rates on the ability of businesses to service their debt continued to be muted, as corporate bonds—which account for the majority of the debt of public firms—generally have fixed interest rates. Although businesses with floating-rate obligations experienced significant increases in interest expenses, earnings were sufficiently strong for most firms to handle these higher interest payments without stress.

Business credit quality declined slightly in 2023. The volume of downgrades exceeded the volume of upgrades, and default rates slightly increased. Nevertheless, both remained low by historical standards. Direct lending to nonfinancial businesses by private credit funds and other private investors grew rapidly. While risks associated with private credit from investor redemption and leverage appeared limited, the sector remains opaque, making it difficult to assess vulnerabilities.

In the household sector, household debt relative to GDP declined in 2023. Mortgage debt accounts for roughly two-thirds of total household debt, with new mortgage extensions skewed toward prime borrowers in recent years. Most of the remaining one-third of household debt is consumer credit, which consists primarily of student loans, auto loans, and credit card debt. Although the strength of households' balance sheets held up through 2023, credit card and auto delinquency rates increased slightly. This increase was likely due to the unwinding of pandemic support programs rather than a significant deterioration in lending standards, which remain conservative. Student loan delinquencies were held down by pandemic-related debt relief. Although the extended pandemic forbearance has ended, the new forgiveness plan of a 12-month "on ramp" to repayment and the new Saving on a Valuable Education plan could temper rising future delinquencies.

Figure 3.5. Common equity tier 1 ratio of banks, 2001–23



Note: The data are seasonally adjusted by Federal Reserve Board staff. Before 2014:Q1, the numerator of the common equity tier 1 ratio is tier 1 common capital for advanced-approaches bank holding companies (BHCs) and intermediate holding companies (IHCs) (before 2015:Q1, for non-advanced-approaches BHCs). Afterward, the numerator is common equity tier 1 capital. The denominator is risk-weighted assets. G-SIBs are global systemically important U.S. banks. Large non–G-SIBs are BHCs and IHCs with greater than $100 billion in total assets that are not G-SIBs. The shaded bars with top caps indicate periods of business recession as defined by the National Bureau of Economic Research: March 2001 to November 2001, December 2007 to June 2009, and February 2020 to April 2020.

Source: Federal Reserve Board, Form FR Y-9C, Consolidated Financial Statements for Holding Companies.

Leverage in the Financial System

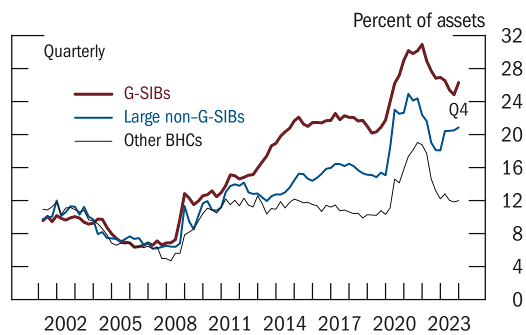
The banking sector remained sound and resilient overall in 2023. Bank runs at Silicon Valley Bank (SVB) and other banks in March 2023 showed that the interaction of fair value losses on bank balance sheets and fragile funding structures could amplify a shock. The use of a systemic risk exception and the Bank Term Funding Program (BTFP) helped mitigate these vulnerabilities and stopped the contagion from bank runs at SVB in March 2023. Common equity tier 1 ratios—regulatory risk-based measures of bank capital adequacy—at the largest banks were near or above the top quartile of their range throughout the past decade (figure 3.5). Nonetheless, fair value losses on fixed-income assets remain sizable at some banks, and there is the potential for weakening loan performance associated with CRE lending to emerge at some lenders. The largest banks appear most resilient to these potential risks. Some smaller banks with less diversified portfolios may face greater challenges.

Outside the banking sector, leverage at large life insurance companies in 2023 remained near the middle of its historical range and well below its pandemic peak. However, life insurance companies continued to increase the share of assets allocated to risky instruments, which leaves their capital positions vulnerable to declines in the value of their investments. Based on a number of measures, leverage at hedge funds during 2023 stabilized at an elevated level as the Treasury cash-futures basis trade continued to grow, suggesting a risk of sudden deleveraging if volatility in Treasury markets increases unexpectedly.

Funding Risk

Overall, banks' liquidity positions remained ample based on the risk of their funding structures. High-quality liquid assets held by banks declined mildly in 2023, driven by reductions in holdings of central bank reserves and by decreases in the market values of securities as interest rates increased. Still, the levels of high-quality liquid assets remained high by historical standards (figure 3.6). The BTFP was created to mitigate funding vulnerabilities of banks amid the stresses of mid-March 2023 and ended on March 11, 2024. A measure of the exposure of banks to interest rate risk—calculated as the difference between the timing of cash flows arising from bank assets and liabilities—declined over the year but remained well above historical levels.

Figure 3.6. Liquid assets held by banks, 2001–23



Note: Liquid assets are cash plus estimates of securities that qualify as high-quality liquid assets as defined by the liquidity coverage ratio requirement. Accordingly, Level 1 assets as well as discounts and restrictions on Level 2 assets are incorporated into the estimate. G-SIBs are global systemically important U.S. banks. Large non–G-SIBs are bank holding companies (BHCs) and intermediate holding companies with greater than $100 billion in total assets that are not G-SIBs.

Source: Federal Reserve Board, Form FR Y-9C, Consolidated Financial Statements for Holding Companies.

Outside the banking sector, assets under management (AUM) of money market funds (MMFs) continued to increase in 2023. Growth in prime MMFs likely reflects faster increases in their yields relative to the yields of other MMFs and deposit rates, as short-term interest rates have risen. Combined AUM in other cash-management vehicles—such as offshore prime MMFs, short-term investment funds, private liquidity funds, and ultrashort bond funds—continued to increase and remained at a historically high level. Rule changes for MMFs by the Securities and Exchange Commission that went into effect in July 2023 represent reforms to address the structural weaknesses in this sector.

After modest outflows in 2023, the total outstanding amount of corporate bonds held by mutual funds fell to its lowest level of the past decade. Bond mutual funds experienced net redemptions throughout the year, which they managed in an orderly manner.

Finally, stablecoin assets remained sizable at around $125 billion. Given their footprint in money market instruments, runs on stablecoins could amplify strains in short-term funding markets. Stablecoins are also used as cash substitutes in crypto trading, which can amplify the risk of disruptive spillovers from the crypto ecosystem to the traditional financial system. The lack of regulatory oversight for stablecoins adds to their vulnerabilities.

Domestic and International Cooperation and Coordination

The Federal Reserve cooperated and coordinated with both domestic and international institutions in 2023 to promote financial stability.

Financial Stability Oversight Council Activities

As mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, the FSOC was created in 2010. The FSOC is chaired by the Secretary of the Treasury and includes the Chair of the Board of Governors of the Federal Reserve System as a member. It established an institutional framework for identifying and responding to sources of systemic risk. Through collaborative participation in the FSOC, U.S. financial regulators monitor not only institutions, but also the financial system as a whole. The Federal Reserve, in conjunction with other participants, assists in monitoring financial risks, analyzing the implications of those risks for financial stability, and identifying steps that can be taken to mitigate those risks. In addition, when the FSOC designates an institution as systemically important, the Federal Reserve assumes responsibility for supervising that institution.

The FSOC continued to serve as a central venue for member agencies to collaborate as well as discuss and assess financial stability risks. In 2023, the council had four areas of priority: (1) nonbank financial intermediation, (2) Treasury market resilience, (3) climate-related financial risk, and (4) digital assets.[3]

The council continued to assess vulnerabilities associated with nonbank financial institutions. The Hedge Fund Working Group (HFWG) has developed an interagency risk-monitoring system to assess the financial stability risks associated with hedge funds. The Nonbank Mortgage Servicing Task Force continued monitoring the financial stability risks posed by nonbank mortgage servicers.

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[3] See Financial Stability Oversight Council, "Minutes of the Financial Stability Oversight Council" (Washington: FSOC, February 10, 2023), https://home.treasury.gov/system/files/261/FSOC_20230210_Minutes.pdf.

The council supported the work of the U.S. Treasury and the Inter-Agency Working Group on Treasury Market Surveillance (IAWG), of which the Federal Reserve is a member, to strengthen the resilience of U.S. Treasury markets. The work of the council's HFWG has informed the IAWG's assessment of how funds' leverage and liquidity risk-management practices affect the U.S. Treasury market.

The council's staff-level Climate-related Financial Risk Committee (CFRC) provided a forum for FSOC members to coordinate and build capacity to identify, measure, and assess climate-related financial stability risks. In July 2023, the CFRC issued a staff progress report providing an update on efforts to advance the recommendations included in the 2021 *Report on Climate-Related Financial Risk*.[4]

Following the publication of its *Report on Digital Asset Financial Stability Risks and Regulation* in 2022, the council's Digital Assets Working Group continued to discuss and analyze developments and risks in the crypto-asset ecosystem.[5]

In 2023, the council issued a new proposed analytical framework for financial stability risks and proposed updated interpretative guidance for designating nonbank financial companies for Federal Reserve supervision and enhanced prudential standards. After releasing the two documents for public comment on April 23, 2023, the council finalized the two documents on November 3, 2023, with approval from the Federal Reserve as a member.[6] The new framework and guidance aim to improve the council's ability to address risks to financial stability and to provide greater public transparency.

The council's 2023 annual report reviewed significant financial market developments, described potential emerging threats to U.S. financial stability, identified vulnerabilities in the financial system, and made recommendations to mitigate them.[7] The report included boxes on the following topics: global economic conditions, household finance, the spring 2023 turmoil and policy responses, Treasury market resilience during March 2023, successful implementation of alterna-

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[4] See Financial Stability Oversight Council, *Climate-related Financial Risk: 2023 Staff Progress Report* (Washington: FSOC, July 28, 2023), https://home.treasury.gov/system/files/261/FSOC-2023-Staff-Report-on-Climate.pdf; and Financial Stability Oversight Council, *Report on Climate-Related Financial Risk* (Washington: FSOC, October 2021), https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf.

[5] See Financial Stability Oversight Council, *Report on Digital Asset Financial Stability Risks and Regulation* (Washington: FSOC, October 2022), https://home.treasury.gov/system/files/261/FSOC-Digital-Assets-Report-2022.pdf.

[6] See Financial Stability Oversight Council, "Analytic Framework for Financial Stability Risk Identification, Assessment, and Response," 88 Fed. Reg. 218 (November 14, 2023): 78,026–37, https://home.treasury.gov/system/files/261/Analytic-Framework-for-Financial%20Stability-Risk-Identification-Assessment-and-Response.pdf; and Financial Stability Oversight Council, "Guidance on Nonbank Financial Company Determinations," 88 Fed. Reg. 221 (November 17, 2023): 80,110–31, https://home.treasury.gov/system/files/261/Interpretive-Guidance-Regarding-Authority-to-Require-Supervision-and-Regulation-of-Certain-Nonbank-Financial-Companies.pdf.

[7] See Financial Stability Oversight Council, *Annual Report* (Washington: FSOC, 2023), https://home.treasury.gov/system/files/261/FSOC2023AnnualReport.pdf.

tive reference rates, speed of financial transactions and information transmission, and quantum computing.

Financial Stability Board Activities

In light of the interconnected global financial system and the global activities of large U.S. financial institutions, the Federal Reserve participates in international bodies, such as the FSB. The FSB monitors the global financial system and promotes international financial stability by coordinating with national financial authorities and international standard-setting bodies on information exchanges and work focused on developing strong global financial-sector policies.

In 2023, the FSB engaged in many issues related to global financial stability. Specific work included addressing structural vulnerabilities from liquidity mismatch in open-end funds, assessing the financial stability implications of multifunction crypto-asset intermediaries, and enhancing the resilience of nonbank financial intermediation.

4 | Supervision and Regulation

The Federal Reserve promotes a safe, sound, and efficient banking and financial system that supports the growth and stability of the U.S. economy. The Federal Reserve carries out its supervisory and regulatory responsibilities and supporting functions primarily by

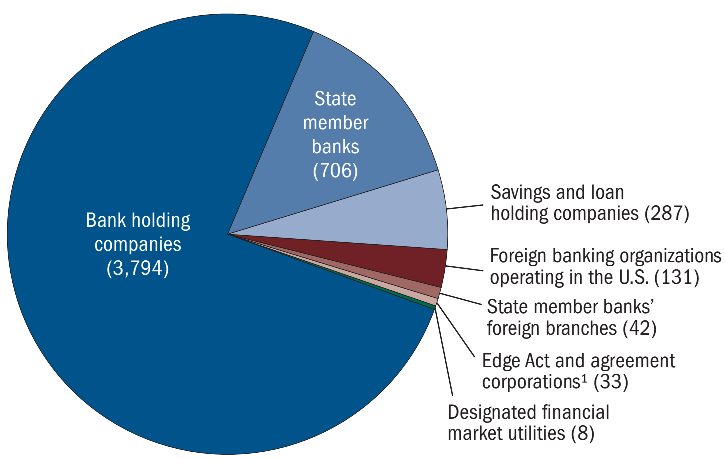
- supervising the activities of financial institutions to promote their safety and soundness (see figure 4.1);
- developing regulatory policy (rulemakings, supervision and regulation letters, policy statements, and guidance) and acting on applications filed by banking organizations; and
- monitoring trends in the banking sector by collecting and analyzing data (see box 4.1).

Box 4.1. Banking Sector Conditions

For information on banking sector conditions, see the *Supervision and Regulation Report*, which is submitted semiannually to the Senate Committee on Banking, Housing, and Urban Affairs and to the House Committee on Financial Services. The reports are available on the Board's website at https://www.federalreserve.gov/publications/supervision-and-regulation-report.htm.

Figure 4.1. The Federal Reserve oversees a broad range of financial entities

Bank holding companies constitute the largest segment of institutions supervised by the Federal Reserve, but the Federal Reserve also supervises state member banks, savings and loan holding companies, foreign banks operating in the United States, and other entities. See "Supervised and Regulated Institutions" in this section.



[1] Edge Act and agreement corporations are subsidiaries of banks or bank holding companies, organized to allow international banking and financial business.

Supervised and Regulated Institutions

The Federal Reserve categorizes banking organizations into portfolios by size and entity type, as described in table 4.1.

State Member Banks

At year-end 2023, a total of 1,411 banks (excluding non-depository trust companies and private banks) were members of the Federal Reserve System, of which 706 were state chartered. Federal Reserve System member banks operated 47,166 branches and accounted for 34 percent of all commercial banks in the United States and 67 percent of all commercial banking offices. State-chartered commercial banks that are members of the Federal Reserve, commonly referred to as state member banks, represented approximately 17 percent of all insured U.S. commercial banks and held approximately 17 percent of all insured commercial bank assets in the United States.

Table 4.1. Summary of supervised institutions

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

* 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.

Bank Holding Companies

At year-end 2023, a total of 3,794 U.S. bank holding companies (BHCs) were in operation, of which 3,407 were top-tier BHCs. These organizations controlled 3,486 insured commercial banks and held approximately 95 percent of all insured commercial bank assets in the United States.

BHCs that meet certain capital, managerial, and other requirements may elect to become financial holding companies (FHCs). FHCs can generally engage in a broader range of financial activities than other BHCs. As of year-end 2023, a total of 502 domestic BHCs and 45 foreign banking organizations had FHC status. Of the domestic FHCs, 23 had consolidated assets of $100 billion or more; 62 between $10 billion and $100 billion; 191 between $1 billion and $10 billion; and 226 less than $1 billion.

Savings and Loan Holding Companies

At year-end 2023, a total of 287 savings and loan holding companies (SLHCs) were in operation, of which 148 were top-tier SLHCs. These SLHCs controlled 160 depository institutions. Approximately 94 percent of SLHCs engage primarily in depository or broker-dealer activities. These firms hold approximately 62 percent ($852.6 billion) of the total combined assets of all SLHCs. The Office of the Comptroller of the Currency (OCC) or the Federal Deposit Insurance Corporation (FDIC) is the primary federal regulator for subsidiary savings associations of SLHCs. Some SLHCs are engaged primarily in nonbanking activities, such as insurance underwriting (5 SLHCs) and commercial activities (4 SLHCs). The 25 largest SLHCs accounted for almost $1.3 trillion of total combined assets.

At year-end 2023, the Federal Reserve supervised five companies that own depository institutions and are significantly engaged in insurance activities. All five of these institutions were SLHCs. As of December 31, 2023, they had approximately $425 billion in total assets. Two of these firms have total assets greater than $100 billion, and insured depository assets represent less than half of total assets for four of the five SLHCs.

In 2022, the Federal Reserve proposed and finalized a supervisory framework for insurance organizations that are overseen by the Board. The supervisory framework consists of a risk-based approach to supervisory expectations and activities; a unique supervisory ratings system; and reliance, to the fullest extent possible, on the work performed by other relevant supervisors, including the state insurance regulators. In 2023, the Federal Reserve made progress in implementing this framework, including by issuing ratings under the new system for four supervised insurance organizations.

Financial Market Utilities

Financial market utilities (FMUs) manage or operate multilateral systems for the purpose of transferring, clearing, or settling payments, securities, or other financial transactions among financial institutions or between financial institutions and the FMU. The Federal Reserve supervises FMUs that are chartered as member banks or Edge Act corporations, and coordinates with other federal banking supervisors to supervise FMUs considered bank service providers under the Bank Service Company Act.

In July 2012, the Financial Stability Oversight Council (FSOC) voted to designate eight FMUs as systemically important under title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). As a result of these designations, the Board assumed an expanded set of responsibilities related to these designated FMUs that includes promoting uniform risk-management standards, playing an enhanced role in the supervision of designated FMUs, reducing systemic risk, and supporting the stability of the broader financial system. For certain designated FMUs, the Board established risk-management standards and expectations that are articulated in the Board's Regulation HH.

In addition to setting minimum risk-management standards, Regulation HH establishes advance notice requirements for proposed material changes to the rules, procedures, or operations of a designated FMU for which the Board is the supervisory agency under title VIII. Finally, Regulation HH also establishes minimum conditions and requirements for a Federal Reserve Bank to establish and maintain an account for, and provide services to, a designated FMU.[1] Where the Board is not the title VIII supervisory agency, the Federal Reserve works closely with the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission to promote robust FMU risk management and monitor systemic risks across the designated FMUs.

International Activities

Foreign operations of U.S. banking organizations. At the end of 2023, a total of 21 member banks were operating 251 branches in foreign countries and overseas areas of the United States. Ten national banks were operating 197 of these branches, 11 state member banks were operating 42 of these branches, and 5 nonmember banks were operating the remaining 12.

Edge Act and agreement corporations. At year-end 2023, out of 33 banking organizations chartered as Edge Act or agreement corporations, 3 operated 6 Edge Act and agreement branches. These corporations are examined annually.

U.S. activities of foreign banks. As of year-end 2023, a total of 131 foreign banks from 47 countries operated 139 state-licensed branches and agencies, of which 6 were insured by the FDIC, and 48 OCC-licensed branches and agencies, of which 4 were insured by the FDIC. These foreign banks also owned six Edge Act and agreement corporations. In addition, they held a controlling interest in 33 U.S. commercial banks. Altogether, the U.S. offices of these foreign banks controlled approximately 17.8 percent of U.S. commercial banking assets. These 131 foreign banks

[1] The Federal Reserve Banks maintain accounts for and provide services to several designated FMUs.

also operated 88 representative offices; an additional 32 foreign banks operated in the United States through a representative office.

The Federal Reserve conducted or participated with state and federal regulatory authorities in 684 examinations of foreign banks in 2023.

Box 4.2. Failure of Silicon Valley Bank and the Federal Reserve's Response

Following the failures of Silicon Valley Bank (SVB) and Signature Bank in March 2023, the Federal Reserve took action to respond to the current banking conditions and contagion risk across the financial system, including enhancing monitoring of firms with similar risk profiles.

Immediately after SVB's failure, Chair Jerome Powell and Vice Chair for Supervision Michael Barr agreed that Vice Chair for Supervision Barr should lead a review of the failure, and on April 28, 2023, the results of that review were published. The report provided a review of the factors that contributed to the failure of SVB. The report showed that SVB was a highly vulnerable firm in ways that were not fully appreciated by the firm's board of directors, senior management, and Federal Reserve supervisors. These vulnerabilities—foundational and widespread managerial weaknesses, a highly concentrated business model, and a reliance on uninsured deposits—left SVB exposed to the specific combination of rising interest rates and slowing activity in the technology sector that materialized in 2022 and early 2023.

The failure of SVB and the ensuing stress in the banking system highlighted the need to improve the speed, force, and agility of supervision to align better with the risks, size, and complexity of supervised banks, as appropriate. The Federal Reserve has been working to ensure supervision intensifies at the right pace as a bank grows in size and complexity, to modify supervisory processes so that issues, once identified, are addressed more quickly by both banks and supervisors, and to find better ways to incorporate forward-looking analysis into supervision.

Supervisory Developments

Supervisory and Regulatory Initiatives

The Federal Reserve's supervision activities include examinations and inspections to help ensure that financial institutions operate in a safe and sound manner and comply with laws and regulations, including consumer protection. These include an assessment of a financial institution's risk-management systems, financial conditions, governance and controls, and compliance. The Federal Reserve tailors its supervisory approach based on the size and complexity of firms. Supervisory oversight ranges from a continuous supervisory presence with dedicated teams of examiners for large firms to regular point-in-time and targeted periodic examinations for small, noncomplex firms.

Supervisory priorities are focused on both previously identified supervisory findings and emerging concerns arising from changing economic conditions. Examiners monitor and assess a supervised institution's remediation of supervisory findings in areas, such as independent risk management and controls, compliance, operational and cyber resilience, and information technology.

In 2023, the Federal Reserve conducted 316 examinations of state member banks, 2,894 inspections of bank holding companies, and 120 inspections of savings and loan holding companies.

Tables 4.2 and 4.3 provide information on examinations and inspections conducted by the Federal Reserve during the past five years. Additionally, the Federal Reserve took a number of actions, including enhanced monitoring to stabilize the banking environment after two bank failures (box 4.2).

Table 4.2. Savings and loan holding companies, 2019–23

Entity/item	2023	2022	2021	2020	2019
Top-tier savings and loan holding companies					
Assets of more than $1 billion					
Total number	48	50	47	50	53
Total assets (billions of dollars)	1,334	1,741	1,856	2,026	1,822
Number of inspections	51	50	63	55	52
By Federal Reserve System	51	50	63	55	52
Assets of $1 billion or less					
Total number	100	102	107	119	134
Total assets (billions of dollars)	39	36	37	39	39
Number of inspections	69	74	78	91	102
By Federal Reserve System	69	74	78	91	102

Table 4.3. State member banks and bank holding companies, 2019–23

Entity/item	2023	2022	2021	2020	2019
State member banks					
Total number	706	701	705	734	754
Total assets (billions of dollars)	3,894	3,997	4,016	3,568	2,642
Number of examinations	559	524	471	502	554
By Federal Reserve System	316	289	288	263	327
By state banking agency	243	235	183	239	227
Top-tier bank holding companies					
Assets of more than $1 billion					
Total number	824	809	795	746	631
Total assets (billions of dollars)	25,979	25,275	25,185	23,811	20,037
Number of inspections	1,051	966	996	875	805
By Federal Reserve System[1]	989	891	919	814	761
By state (or other) banking agency	62	75	77	61	44
Assets of $1 billion or less					
Total number	2,613	2,672	2,762	2,887	3,094
Total assets (billions of dollars)	886	883	900	883	870
Number of inspections	1,694	1,768	1,801	1,967	2,122
By Federal Reserve System	1,589	1,699	1,727	1,890	2,033
By state (or other) banking agency	106	69	74	77	89
Financial holding companies					
Domestic	502	505	504	502	493
Foreign	45	46	45	44	44

[1] For bank holding companies subject to continuous, risk-focused supervision, includes multiple targeted reviews.

Specialized Examinations

The Federal Reserve conducts specialized examinations of supervised financial institutions in the areas of capital planning and stress testing, information technology, fiduciary activities, transfer agent activities, government and municipal securities dealing and brokering, and cybersecurity and critical infrastructure. The Federal Reserve also conducts specialized examinations of certain non-bank entities that extend credit subject to the Board's margin regulations.

Capital Planning and Stress Testing

Since the 2007–09 financial crisis, the Federal Reserve has instituted supervisory stress testing to strengthen capital positions of the largest banking organizations. In March 2020, the Board integrated the supervisory stress test with its non-stress capital requirements through the stress capital buffer to form one forward-looking and risk-sensitive capital framework.

In June 2023, the Federal Reserve conducted its annual stress test, which showed that the large banking firms tested had sufficient levels of capital and could continue lending to households and businesses during a severe recession. In July 2023, the Federal Reserve announced the individual capital requirements for large banks, which include the stress capital buffer requirement based on the results of the 2023 stress test. These requirements became effective as of October 1, 2023.

For the first time, the Federal Reserve also published an exploratory market shock that applied only to U.S. global systemically important banks and posed a different set of risks than the global market shock component.[2] Consistent with the nature of an exploratory exercise, the exploratory market shock did not contribute to the capital requirements set by the 2023 stress test. For stress testing publications released in 2023, see box 4.3.

Box 4.3. Stress Testing Publications Released in 2023

More details on the 2023 stress test scenarios are available at https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20230209a1.pdf.

More details on the 2023 stress test model methodologies are available at https://www.federalreserve.gov/publications/files/2023-june-supervisory-stress-test-methodology.pdf.

More details on the 2023 stress test results are available at https://www.federalreserve.gov/publications/files/2023-dfast-results-20230628.pdf.

More details on the stress capital buffer requirements published in 2023 are available at https://www.federalreserve.gov/publications/files/large-bank-capital-requirements-20230727.pdf

[2] The global market shock applies to banks with large trading operations and stresses their trading, private equity, and certain other fair-valued positions. It consists of a set of hypothetical shocks to a large set of risk factors reflecting general market distress and heightened uncertainty. Banks with substantial trading or custodial operations are also tested against the default of their largest counterparty.

Fiduciary Activities

In 2023, Federal Reserve examiners conducted 73 fiduciary examinations of state member banks and non-depository trust companies.

Transfer Agents

During 2023, the Federal Reserve conducted transfer agent examinations at three state member banks and two BHCs that were registered as transfer agents.

Government and Municipal Securities Dealers and Brokers

The Federal Reserve is responsible for examining state member banks and foreign banks for compliance with the Government Securities Act of 1986 and with the U.S. Treasury regulations governing dealing and brokering in government securities. During 2023, the Federal Reserve conducted eight examinations of government securities activities at these organizations.

The Federal Reserve is also responsible for ensuring that state member banks and BHCs that act as municipal securities dealers comply with the Securities Act Amendments of 1975. Municipal securities dealers are examined, pursuant to the Municipal Securities Rulemaking Board's rule G-16, at least once every two calendar years. During 2023, the Federal Reserve examined six entities that dealt in municipal securities.

Securities Credit Lenders

Under the Securities Exchange Act of 1934, the Board is responsible for regulating credit in certain transactions involving the purchasing or carrying of securities. As part of its general examination program, the Federal Reserve examines the banks under its jurisdiction for compliance with the Board's Regulation U. In addition, the Federal Reserve maintains a registry of persons other than banks, brokers, and dealers who extend credit subject to Regulation U. Throughout the year, Federal Reserve examiners conducted specialized examinations of these lenders if they are not already subject to supervision by the Farm Credit Administration or the National Credit Union Administration.

Operational Resilience, Information Technology, and Cybersecurity

Effective operational risk management and resilience are vital to the safety and soundness of financial institutions and the stability of the U.S. financial system.[3] The Federal Reserve provides guidance, tools, and educational resources to assist supervised institutions in managing such risks.

[3] Operational risk management includes risk management of information technology, cyber, and third-party risks.

In June 2023, the Board, the FDIC, and the OCC issued the Interagency Guidance on Third-Party Relationships: Risk Management that describes principles and considerations for banking organizations' risk management of third-party relationships, including key considerations for cybersecurity and operational risks associated with such relationships.

In July 2023, staff from the Board and other federal banking agencies conducted an "Ask the Regulator" session to highlight key aspects of the third-party risk-management guidance and its application to banks. In November 2023, Board staff conducted an "Ask the Fed" session to address questions about the guidance from banks, including smaller banks.

The Federal Reserve examined and monitored supervised institutions for operational risks as part of its safety and soundness supervision:

- In 2023, Federal Reserve examiners, in close coordination with the other federal banking agencies, conducted examinations of IT activities (inclusive of cyber risk-management activities) and targeted cybersecurity assessments of the large financial institutions, and service providers.
- Federal Reserve examiners also conducted tailored cybersecurity assessments at community and regional banking organizations.
- Under the authority of the Bank Service Company Act, the federal banking agencies examined technology service providers that provide services for specific regulated financial institutions.

The Federal Reserve collaborated with other financial regulators, U.S Treasury, and private industry to promote effective safeguards against operational and cyber risks to the financial services sector and its critical infrastructure. This included contributions to the Federal Financial Institutions Examination Council's (FFIEC's) IT Subcommittee and Cybersecurity and Critical Infrastructure Subcommittee, the Financial and Banking Information Infrastructure Committee, the Cybersecurity Forum for Independent and Executive Branch Regulator, the Department of Homeland Security's Cybersecurity and Infrastructure Security Agency Cyber Incident Reporting Council, and Cyber Incident Reporting for Critical Infrastructure Act-related deliberations. The Federal Reserve, together with the other members of the Financial Banking Information Infrastructure Committee (FBIIC) and the Financial Services Sector Coordinating Council, collaborated on financial sector resilience initiatives, including participation in the Cloud Executive Steering Group.[4]

The Board led or contributed to cybersecurity activities undertaken by various international groups. Board staff continued to participate in the work of the Financial Stability Board (FSB) to address

[4] See U.S. Department of the Treasury, "U.S. Department of the Treasury Kicks Off Public–Private Executive Steering Group to Address Cloud Report Recommendations," news release, May 25, 2023, https://home.treasury.gov/news/press-releases/jy1503. The Federal Reserve and other members of the FBIIC contributed to a Treasury report that assesses the opportunities and challenges the financial sector faces by adopting cloud-based technologies, in which this working group was first announced.

current and emerging operational risks. This resulted in the publication of the policy documents, "Enhancing Third-Party Risk Management and Oversight: A toolkit for financial institutions and financial authorities" and "Recommendations to Achieve Greater Convergence in Cyber Incident Reporting: Final Report.[5]

Crypto-Asset Supervision

Novel Activities Supervision Program

In 2023, the Federal Reserve System launched the Novel Activities Supervision Program to enhance the supervision of novel activities conducted by banking organizations supervised by the Federal Reserve.[6] The goal of the program is to foster innovation at banking organizations while recognizing and appropriately addressing risks to help ensure the safety and soundness of the banking system. The program focuses on novel activities related to crypto-assets; distributed ledger technology; and complex, technology-driven partnerships with nonbanks to deliver financial services to customers.

The Federal Reserve established this program with dedicated staff to maintain strong and consistent oversight of novel activities at supervised institutions, and to help ensure that the novel risks associated with innovation are appropriately addressed. By bringing together staff focused on novel activities, the Federal Reserve's knowledge of these activities can grow more rapidly and continue to build upon and enhance technical expertise related to novel activities. The program will also inform the development of supervisory approaches and guidance for banking organizations engaging in novel activities, as warranted.

Crypto-Related Activities

In 2023, the Federal Reserve issued a number of statements with respect to banking organizations' engagement in crypto-asset related activities and with the crypto-sector. On January 3, 2023, the Federal Reserve, the OCC, and the FDIC issued a joint statement of key risks associated with crypto-assets and crypto-asset sector participants that banking organizations should be aware of. The highlighted risks included fraud and scams; legal uncertainties; inaccurate or misleading representations and disclosures; volatility; runs on stablecoins; interconnectedness among crypto-asset participants; immature governance and risk management practices; and heightened risks associated with open, public, and/or decentralized networks, among others.

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5 See Financial Stability Board, *Final Report on Enhancing Third-Party Risk Management and Oversight – A Toolkit for Financial Institutions and Financial Authorities* (Basel: FSB, December 2023), https://www.fsb.org/2023/12/final-report-on-enhancing-third-party-risk-management-and-oversight-a-toolkit-for-financial-institutions-and-financial-authorities/ and *Recommendations to Achieve Greater Convergence in Cyber Incident Reporting: Final Report* (Basel: FSB, April 2023), https://www.fsb.org/2023/04/recommendations-to-achieve-greater-convergence-in-cyber-incident-reporting-final-report/.

6 See https://www.federalreserve.gov/publications/files/202311-supervision-and-regulation-report.pdf.

On February 23, the agencies issued a second statement focused on liquidity risk and the potential volatility of funding inflows and outflows associated with crypto-asset activity. On August 8, 2023, the Federal Reserve published SR letter 23-08/CA letter 23-08, "Supervisory Nonobjection Process for State Member Banks Seeking to Engage in Certain Activities Involving Dollar Tokens," describing the process through which state member banks may seek a supervisory nonobjection before conducting certain activities involving "dollar tokens."[7] The supervisory nonobjection expectation was first articulated in the Board's January 27, 2023, Policy Statement on section 9(13) of the Federal Reserve Act (Policy Statement).[8] The SR letter does not create any new substantive expectations but lays out the process state member banks should follow to obtain such supervisory nonobjection. The letter notes that Federal Reserve staff will focus on operational, cyber security, liquidity, illicit finance, and consumer compliance risks.

Climate-Related Financial Risks

In 2023, the Board launched a pilot Climate Scenario Analysis exercise to learn about large banking organizations' climate risk-management practices and challenges and to enhance the ability of both large banking organizations and supervisors to identify, measure, monitor, and manage climate-related financial risks. As described in the *Participant Instructions* released on January 17, 2023, the exercise considered the impact of physical and transition risk scenarios of varying levels of severity on participating banks' balance sheets. The exercise was exploratory in nature and does not have consequences for bank capital or supervisory implications.[9]

On October 24, 2023, the Board, along with other federal banking regulatory agencies, finalized principles that provide a high-level framework for the safe and sound management of exposures to climate-related financial risks for large financial institutions.[10] The principles are intended for institutions with $100 billion or more in total assets and address physical and transition risks associated with climate change. General climate-related financial risk management principles are provided with respect to a financial institution's governance; policies, procedures, and limits; strategic planning; risk management; data, risk measurement, and reporting; and scenario analysis. Additionally, the principles describe how climate-related financial risks can be addressed in the management of traditional risk areas, including credit, market, liquidity, operational, and legal risks.

Enforcement Actions

The Federal Reserve has enforcement authority over the financial institutions it supervises and their affiliated parties. Enforcement actions may be taken to address unsafe or unsound practices and violations of law or regulation. Formal enforcement actions include cease and desist orders,

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[7] See https://www.federalreserve.gov/supervisionreg/srletters/SR2308.htm.
[8] See https://www.federalreserve.gov/newsevents/pressreleases/bcreg20230127a.htm.
[9] See https://www.federalreserve.gov/publications/climate-scenario-analysis-exercise-instructions.htm.
[10] See https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231024b.htm.

written agreements, prompt corrective action directives, removal and prohibition orders, civil money penalties, and letters sent pursuant to 12 U.S.C. § 1829, known as Section 19 letters.

In 2023, the Federal Reserve completed 63 formal enforcement actions. Civil money penalties totaling $542,329,952.20 were assessed. As directed by statute, all civil money penalties are remitted to either the U.S. Treasury or the Federal Emergency Management Agency. The Reserve Banks completed 99 informal enforcement actions. Informal enforcement actions include memoranda of understanding, commitment letters, supervisory letters, and board of directors' resolutions.

Enforcement orders and prompt corrective action directives, which are issued by the Board, and written agreements, which are executed by the Reserve Banks, are made public and are posted on the Board's website (https://www.federalreserve.gov/apps/enforcementactions/search.aspx).

The Federal Reserve's enforcement responsibilities also extend to the disclosure of financial information by state member banks and the use of credit to purchase and carry securities.

Financial Disclosures by State Member Banks

Under the Securities Exchange Act of 1934 and the Federal Reserve's Regulation H, certain state member banks are required to make financial disclosures to the Federal Reserve using the same reporting forms that are normally used by publicly held entities to submit information to the SEC.[11]

In 2023, one state member bank was required to submit data to the Federal Reserve. These data are made available upon request and are primarily used for disclosure to the bank's shareholders and public investors.

Internal Appeals of Material Supervisory Determinations

The Board is committed to maintaining an independent, intra-agency process to review appeals of material supervisory determinations (MSD) that complies with section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994.[12] The appeals process includes two levels of review. A panel of Reserve Bank staff who are not employed by the Reserve Bank with supervisory responsibility of the financial institution that issued the appealed MSD conducts the initial review. This panel determines whether the appealed MSD is consistent with applicable laws, regulations, and policy, and is supported by a preponderance of the evidence in the record. If the

[11] Under section 12(g) of the Securities Exchange Act, certain companies that have issued securities are subject to SEC registration and filing requirements that are similar to those that apply to public companies. Per section 12(i) of the Securities Exchange Act, the powers of the SEC over banking entities that fall under section 12(g) are vested with the appropriate banking regulator. Specifically, state member banks with 2,000 or more shareholders and more than $10 million in total assets are required to register with, and submit data to, the Federal Reserve. For more information on the Board's Regulation H policy action, see appendix E, "Record of Policy Actions."

[12] U.S.C. § 4806.

appealing institution is not satisfied with the initial review panel's decision, the institution may request a final review of the MSD. A panel of senior Board staff conducts the final review. The final review panel determines whether the decision of the initial review panel is reasonable. Additional information is available regarding the Federal Reserve Board's appeals process and Ombuds policy.[13]

In 2023, the Board received one MSD appeal from a state member community banking organization. The Board also granted one request for an extension to file an appeal from another state member community banking organization.

Assessments for Supervision and Regulation

BHCs and SLHCs with total consolidated assets of $100 billion or more, as well as any nonbank financial companies designated by the FSOC for supervision by the Board, are subject to assessments for the cost of the Board's supervision and regulation. As a collecting entity, the Board does not recognize the supervision and regulation assessments as revenue nor does the Board use the collections to fund Board expenses; the funds are transferred to the U.S. Treasury. The Board collected and transferred to the U.S. Treasury $771,050,870 from 53 institutions for the 2022 S&R Regulation TT assessment in 2023.

Training and Technical Assistance

The Federal Reserve provides training and technical assistance to foreign supervisors and minority-owned depository institutions as well as engages in industry outreach in connection with supervisory objectives.

International Training and Technical Assistance

In 2023, the Federal Reserve continued to provide training and technical assistance on supervisory matters to foreign central banks and supervisory authorities. Technical assistance normally involves visits by Federal Reserve staff members to foreign authorities as well as consultations with foreign supervisors who visit the Board of Governors or the Reserve Banks. The Federal Reserve organized 20 training seminars, held both onshore and overseas, for the benefit of foreign supervisory authorities. Approximately 900 financial institution supervisors from foreign central banks and supervisory agencies attended these training events during 2023.

Federal Reserve staff also collaborated with the International Monetary Fund and the World Bank to organize two training events for senior supervisory officials. Other training partners that collaborated with the Federal Reserve during 2023 to organize training events included the Association of

[13] See https://www.federalreserve.gov/supervisionreg/srletters/SR2028.htm and https://www.federalreserve.gov/aboutthefed/ombpolicy.htm.

Bank Supervisors of the Americas, the National Banking and Securities Commission of Mexico, and the European Central Bank.

Efforts to Support Minority-Owned Depository Institutions

The Federal Reserve System implements its responsibilities under section 367 of the Dodd-Frank Act primarily through its Partnership for Progress (PFP) program.[14] Established in 2008, this program promotes the viability of minority depository institutions (MDIs) by facilitating activities designed to strengthen their business strategies, maximize their resources, and increase their awareness and understanding of supervisory expectations. The program supports an inclusive financial system and helps facilitate access to credit and other financial services in traditionally underserved areas.

The Federal Reserve maintains the PFP website, which supports MDIs by providing them with technical information and links to useful resources.[15] Representatives from each of the 12 Federal Reserve Districts, along with staff from the Divisions of Supervision & Regulation and Consumer & Community Affairs at the Board of Governors, continue to offer technical assistance tailored to MDIs by providing targeted supervisory guidance, identifying additional resources, and fostering mutually beneficial partnerships between MDIs and community organizations. As of year-end 2023, the Federal Reserve's MDI portfolio consisted of 16 state member banks.

Throughout 2023, the System supported MDIs and conducted a number of outreach initiatives, webinars, and conferences specific to MDIs, including the following:

- *2023 Interagency Minority Depository Institution and CDFI Bank Conference:* The Federal Reserve along with the FDIC and OCC, hosted the biennial interagency conference for MDI and Community Development Financial Institution (CDFI) banks on November 15–16, 2023, at the Federal Reserve Bank of Dallas. The conference theme was "MDI and CDFI Bank Partnership Exchange" and focused on collaboration, partnership, and promoting the mission of MDIs and CDFIs among leaders at these institutions.
- *September 2023 Minorities in Banking Forum*: The Federal Reserve Bank of Dallas hosted the System's annual Minorities in Banking Forum on September 27–28, 2023. This forum was for mid-level and senior banking leaders in the financial services industry and focused on leadership, diversity, and career enhancement.

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[14] Section 367 of the Dodd-Frank Act requires the Board to submit an annual report to Congress detailing the actions taken to fulfill the requirements outlined in section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989, as amended by the Dodd-Frank Act in 2010. In addition to the annual reporting requirement, FIRREA section 308 requires the Federal Reserve System to devote efforts toward preserving and promoting minority ownership of MDIs. See also "Annual Report on Promoting Minority Depository Institutions," Board of Governors of the Federal Reserve System, last modified December 21, 2023, https://www.federalreserve.gov/publications/preserving-minority-depository-institutions.htm.

[15] See https://www.fedpartnership.gov.

- *National Bankers Association:* Board staff represented PFP at the National Bankers Association conference in Washington, D.C. The conference focused on building partnerships, technology, capital, and deposits.
- *Bank Term Funding Program:* The PFP team hosted a special "Ask the Fed" webinar on the Bank Term Funding Program for MDIs and CDFIs.
- *Emergency Capital Investment Program (ECIP):*[16] The PFP, along with the FDIC and OCC, hosted an ECIP Interagency Webinar to provide MDIs with technical assistance on supervisory expectations for ECIP recipients.

International Engagement

As a member of the FSB and several international financial standard-setting bodies, the Federal Reserve actively participates in efforts to share information and advance sound supervisory policies for internationally active financial organizations and to enhance the strength, stability, and resilience of the international financial system.

Financial Stability Board

In 2023, the Federal Reserve continued its participation in a variety of activities of the FSB, an organization whose mission is to promote international financial stability. The FSB helps coordinate the work of national financial authorities and international standard-setting bodies and shares information on supervisory and regulatory practices. Priority areas for the year included enhancing cross-border payments, finalizing recommendations for regulating and supervising crypto-assets and stablecoins, revising recommendations to address vulnerabilities of open-ended funds, and developing a toolkit for enhancing third-party risk management and oversight. The full range of the Federal Reserve's FSB activities is discussed in section 3, "Financial Stability."

The FSB also produces a variety of publications, including progress reports, monitoring reports, guidance, consultative documents, and compendia of better practice. Examples issued in 2023 include

- *The Financial Stability Risks of Decentralised Finance* (issued in February and available at https://www.fsb.org/2023/02/the-financial-stability-risks-of-decentralised-finance/)
- *The Financial Stability Aspects of Commodities Markets* (issued in February and available at https://www.fsb.org/2023/02/the-financial-stability-aspects-of-commodities-markets/)
- *High-level Recommendations for the Regulation, Supervision and Oversight of Crypto-Asset Activities and Markets: Final Report* (issued in July and available at https://www.fsb.org/2023/07/high-level-recommendations-for-the-regulation-supervision-and-oversight-of-crypto-asset-activities-and-markets-final-report/)

[16] Established by the Consolidated Appropriations Act, 2021, the Emergency Capital Investment Program (ECIP) was created to encourage low- and moderate-income community financial institutions to augment their efforts to support small businesses and consumers in their communities. Under the program, the U.S. Treasury Department provided nearly $9 billion in capital directly to depository institutions that are certified CDFIs or MDIs.

- *The Financial Stability Implications of Leverage in Non-Bank Financial Intermediation* (issued in September and available at https://www.fsb.org/2023/09/the-financial-stability-implications-of-leverage-in-non-bank-financial-intermediation/)
- *Annual Progress Report on Meeting the Targets for Cross-Border Payments: 2023 Report on Key Performance Indicators* (issued in October and available at https://www.fsb.org/2023/10/annual-progress-report-on-meeting-the-targets-for-cross-border-payments-2023-report-on-key-performance-indicators/)
- *Final Report on Enhancing Third-Party Risk Management and Oversight – A Toolkit for Financial Institutions and Financial Authorities* (issued in December and available at https://www.fsb.org/2023/12/final-report-on-enhancing-third-party-risk-management-and-oversight-a-toolkit-for-financial-institutions-and-financial-authorities/)
- *Revised Policy Recommendations to Address Structural Vulnerabilities from Liquidity Mismatch in Open-Ended Funds* (issued in December and available at https://www.fsb.org/2023/12/revised-policy-recommendations-to-address-structural-vulnerabilities-from-liquidity-mismatch-in-open-ended-funds/)

A comprehensive list of FSB publications is available at https://www.fsb.org/publications.

Basel Committee on Banking Supervision

During 2023, the Federal Reserve contributed to Basel Committee on Banking Supervision (BCBS) supervisory policy recommendations, reports, papers, and consultations designed to improve the supervision of banking organizations' practices.[17] In 2023, the BCBS was particularly focused on supporting the implementation of Basel III reforms, reviewing the 2023 banking turmoil, analyzing the digitalization of finance, and tracking emerging risks to the banking system.

Examples of final BCBS documents issued in 2023 include

- *Progress in Adopting the Principles for Effective Risk Data Aggregation and Risk Reporting* (issued in November and available at https://www.bis.org/bcbs/publ/d559.htm)
- *Newsletter on the Implementation of the Principles for the Effective Management and Supervision of Climate-Related Financial Risks* (issued in November and available at https://www.bis.org/publ/bcbs_nl33.htm)
- *Finalisation of Various Technical Amendments* (issued in November and available at https://www.bis.org/bcbs/publ/d557.htm)
- *Report on the 2023 Banking Turmoil* (issued in October and available at https://www.bis.org/bcbs/publ/d555.htm)

[17] The BCBS provides a forum for regular cooperation on banking supervisory matters. Its 45 members comprise central banks and bank supervisors from 28 jurisdictions.

- *Basel III Monitoring Report* (issued in September and available at https://www.bis.org/bcbs/publ/d554.htm)
- *Newsletter on Credit Risk Issues* (issued in July and available at https://www.bis.org/publ/bcbs_nl32.htm)

Examples of consultative BCBS documents issued in 2023 include

- *Recalibration of Shocks for Interest Rate Risk in the Banking Book* (issued in December and available at https://www.bis.org/bcbs/publ/d561.htm)
- *Disclosure of Climate-Related Financial Risks* (issued in November and available at https://www.bis.org/bcbs/publ/d560.htm)
- *Disclosure of Cryptoasset Exposures* (issued in October and available at https://www.bis.org/bcbs/publ/d556.htm)
- *Core Principles for Effective Banking Supervision* (final consultation issued in July and available at https://www.bis.org/bcbs/publ/d551.htm)

A comprehensive list of BCBS publications is available at https://www.bis.org/bcbs/publications.htm.

Committee on Payments and Market Infrastructures

In 2023, the Federal Reserve continued its active participation in the activities of the Committee on Payments and Market Infrastructures (CPMI), a forum in which central banks promote the safety and efficiency of payment, clearing and settlement activities, and related arrangements.

The CPMI continued to coordinate with the FSB to advance the G-20 priority to enhance global cross-border payments. In 2023, the program moved into a phase focused on practical improvements. In this phase, the CPMI's focus was to encourage and facilitate action by both the public and private sectors as well as facilitate collaboration and engagement with a broad group of stakeholders.

In addition, in conducting its work on financial market infrastructure and market-related reforms, the CPMI often coordinated with the International Organization of Securities Commissions (IOSCO). Over the course of 2023, CPMI-IOSCO advanced work on practices for addressing non-default losses at CCPs and margining practices. In addition, CPMI-IOSCO continued to monitor implementation of the Principles for Financial Market Infrastructures.

Some examples of 2023 CPMI publications include

- *Exploring Multilateral Platforms for Cross-Border Payments* (published by CPMI, the BIS Innovation Hub, the International Monetary Fund, and the World Bank in January and available at https://www.bis.org/cpmi/publ/d213.pdf)

- *Operational and Technical Considerations for Extending and Aligning Payment System Operating Hours for Cross-Border Payments: An Analytical Framework* (published by CPMI in February and available at https://www.bis.org/cpmi/publ/d214.pdf)
- *Facilitating Increased Adoption of Payment Versus Payment (PvP)* (published by CPMI in March and available at https://www.bis.org/cpmi/publ/d216.pdf)
- *Margin Dynamics in Centrally Cleared Commodities Markets in 2022* (published by CPMI, IOSCO, and BCBS in May and available at https://www.bis.org/bcbs/publ/d550.pdf)
- *Report on Current Central Counterparty Practices to Address Non-Default Losses* (published by CPMI and IOSCO in August and available at https://www.bis.org/cpmi/publ/d217.pdf)
- *Harmonised ISO 20022 Data Requirements for Enhancing Cross-Border Payments* (published by CPMI in October and available at https://www.bis.org/cpmi/publ/d218.pdf)
- *Considerations for the Use of Stablecoin Arrangements in Cross-Border Payments* (published by CPMI in October and available at https://www.bis.org/cpmi/publ/d220.pdf)

Example of a consultative CPMI document issued in 2023 include

- *Linking Fast Payment Systems Across Borders: Considerations for Governance and Oversight* (published by CPMI in October and available at https://www.bis.org/cpmi/publ/d219.pdf)

A comprehensive list of CPMI publications is available at https://www.bis.org/cpmi_publs/.

International Association of Insurance Supervisors

The Federal Reserve continued its participation in 2023 in the development of international supervisory standards for the insurance industry. The Federal Reserve participates actively in standard-setting at the International Association of Insurance Supervisors (IAIS) in consultation and collaboration with state insurance regulators, the National Association of Insurance Commissioners, and the Federal Insurance Office. The Federal Reserve's participation focuses on those aspects most relevant to financial stability and standards that have the potential to significantly impact the U.S. insurance market.

In 2023, the IAIS made progress on several initiatives. The IAIS finalized the criteria for assessing whether the Aggregation Method provides comparable outcomes to the Insurance Capital Standard (ICS), consulted on several associated ICPs, and progressed work on incorporating climate risk guidance into certain ICPs.

Examples of IAIS documents issued in 2023 include

- *Issues Paper on Roles and Functioning of Policyholder Protection Schemes (PPSs)* (issued in December and available at https://www.iaisweb.org/2023/12/iais-publishes-issues-paper-on-roles-and-functioning-of-policyholder-protection-schemes-ppss/)

- *Public Consultation on Insurance Capital Standard as a Prescribed Capital Requirement* (issued in June and available at https://www.iaisweb.org/uploads/2023/06/ICS-as-a-PCR-Public-consultation-document.pdf)
- *Explanatory Note on the Final Criteria for the Aggregation Method Comparability Assessment* (issued in March and available at https://www.iaisweb.org/uploads/2023/03/explanatory-note-on-the-final-criteria-for-the-aggregation-method-comparability-assessment.pdf)
- *Public Consultation on ICP 14 (Valuation) and ICP 17* (Capital Adequacy) (issued in June and available at https://www.iaisweb.org/uploads/2023/06/Draft-Revised-ICP-14.pdf and https://www.iaisweb.org/uploads/2023/06/Draft-Revised-ICP-17.pdf)
- *Public Consultation on Climate Risk Supervisory Guidance – Part One* (issued in March and available at https://www.iaisweb.org/uploads/2023/03/climate-risk-supervisory-guidance-part-one.pdf)

A comprehensive list of IAIS publications is available at https://www.iaisweb.org/publications.

The Federal Reserve's Insurance Policy Advisory Committee (IPAC) continued to provide advice to the Board in 2023 on various matters under consideration at the IAIS among other insurance issues. The IPAC was established by the Economic Growth, Regulatory Relief, and Consumer Protection Act to provide information, advice, and recommendations on international insurance capital standards and other insurance issues.[18] In 2023, the IPAC commented on the IAIS's consultation on the ICS from a U.S. life insurance industry perspective. The IPAC also explored potential liquidity concerns for life insurers due to rising rates. The Working Group concluded that life insurers have strong liquidity positions and that the rising rates were unlikely to cause issues within the industry. Additionally, the IPAC established a Climate Working Group to advise the Board on the climate insurance issues in the United States.

Shared National Credit Program

The Shared National Credit (SNC) program is an interagency review and assessment of risk in the largest and most complex credits shared by multiple regulated financial institutions. The SNC program is governed by an interagency agreement among the Board, FDIC, and OCC. SNC reviews are completed in the first and third quarters of the calendar year. Large agent banks receive two reviews each year, while most other agent banks receive a single review each year.

More information on the 2023 Shared National Credit review is available at https://www.federalreserve.gov/newsevents/pressreleases/bcreg20230224a.htm.

[18] More information on the IPAC can be found at https://www.federalreserve.gov/aboutthefed/ipac.htm.

Bank Secrecy Act and Anti-Money-Laundering Compliance

The Federal Reserve is responsible for examining institutions for compliance with the Bank Secrecy Act (BSA) and applicable anti-money-laundering (AML) laws and regulations and conducts such examinations in accordance with the FFIEC's *Bank Secrecy Act/Anti-Money-Laundering Examination Manual*.

During 2023, the Federal Reserve continued to participate in an ongoing interagency effort to update this manual. Many of the revisions are designed to emphasize and enhance the risk-focused approach to BSA/AML supervision and to continue to provide transparency into the BSA/AML and Office of Foreign Assets Control examination process.

The Anti-Money-Laundering Act of 2020 (AML Act) amended the Bank Secrecy Act, resulting in the most significant revision of the United States' framework for anti-money-laundering and countering the financing of terrorism (AML/CFT) since 2001. The purpose of the act is to improve coordination and information sharing; modernize AML/CFT laws; encourage technological innovations and the adoption of new technology; reinforce the risk-based approach to compliance; and establish uniform beneficial ownership information reporting requirements with a secure, nonpublic database for beneficial ownership information. The Federal Reserve continues to work with the U.S. Treasury, federal banking, and other agencies to implement the relevant sections of the AML Act.

The Federal Reserve continued to participate in the U.S. Treasury-led BSA Advisory Group, which includes representatives of regulatory agencies, law enforcement, and the financial services industry.

International Coordination on Sanctions, Anti-Money-Laundering, and Counter-Terrorism Financing

The Federal Reserve participated in a number of international coordination initiatives related to sanctions, money laundering, and terrorism financing. The Federal Reserve continued to monitor and share information with relevant groups regarding the changing sanctions landscape and, in particular, the ongoing global sanctions resulting from Russia's invasion of Ukraine.

Additionally, the Federal Reserve has a long-standing role in the U.S. delegation to the intergovernmental Financial Action Task Force and its working groups, contributing a banking supervisory perspective to the formulation of international standards. The Federal Reserve also continued to participate in the work of the FSB that resulted in the publication of the October 2023 publication of the G–20 Roadmap for Enhancing Cross-border Payments Consolidated progress report for 2023.[19]

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[19] See https://www.fsb.org/2023/10/g20-roadmap-for-enhancing-cross-border-payments-consolidated-progress-report-for-2023/.