FEDERAL RESERVE BANK OF KANSAS CITY | DECEMBER 15, 2022

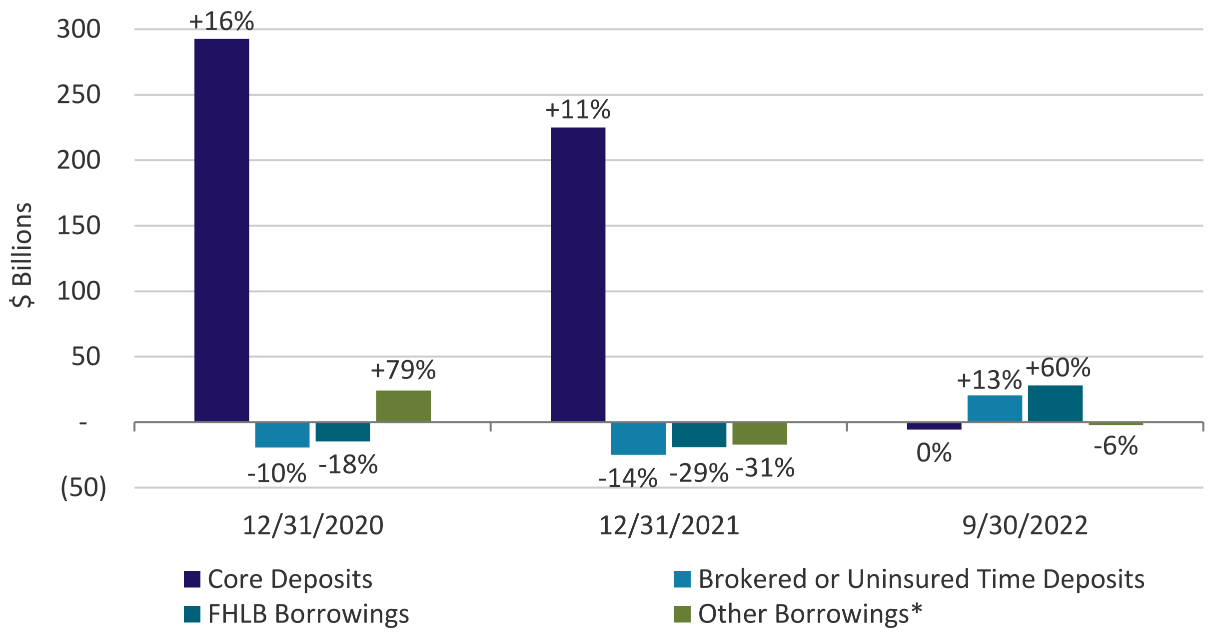
Community Banking Bulletin: Highlight

Providing insights on community banking

Banks turn to noncore borrowings as funding profiles shift

The use of noncore funding has increased in 2022 as banks look to fund loan growth, in contrast to the trends of the prior two years, characterized by large influxes of deposits.

Change in Funding (Year-to-Date)



Note: Other borrowings consist of borrowed funds, excluding those from the Federal Home Loan Banks (FHLB), and includes funds obtained through the Paycheck Protection Program Facility (PPPLF) and Money Market Mutual Fund Liquidity Facility (MMLF), federal funds purchased, and repurchase agreements.
Source: Reports of Condition and Income.

- The funding structure of community banking organizations[1] (CBOs) has shifted throughout the last few years. Following the onset of the COVID-19 pandemic in early 2020, balance sheet trends were largely characterized by extraordinary deposit growth. Core deposits, which exclude brokered deposits or time deposits above the $250,000 insurance limit, grew $518 billion, or 29 percent, across 2020 and 2021.
- As a result of this unprecedented deposit growth, CBOs decreased their reliance on wholesale and noncore funding sources. Specifically, FHLB borrowings and brokered deposits declined 42 percent and 22 percent, respectively, during the same aforementioned two years of strong core deposit growth. However, some banks did take advantage of unique pandemic-era funding programs including the PPPLF and MMLF, accounting for the increase in other borrowings in 2020.
- Beginning in early 2022, funding needs increased due to strong loan growth, and deposit pricing was pressured upwards in line with rising market rates. While CBOs have held an abundance of liquid assets throughout the last few years, many asset-based liquidity options are limited by large unrealized loss positions in available-for-sale securities.[2] As a result of these trends, banks have taken on more noncore funding this year. CBOs have primarily looked to short-term[3] FHLB borrowings and brokered deposits, which have increased $32 billion and $22 billion, respectively, year-to-date.

Questions or comments? Please contact KC.SRM.SRA.CommunityBankingBulletin@kc.frb.org

[1] Community banking organizations are defined as having $10 billion or less in total assets.
[2] See recent CBB discussing how the current rising rate environment has resulted in growing unrealized loss positions.
[3] Includes FHLB advances with a remaining maturity or next repricing date of one year or less.