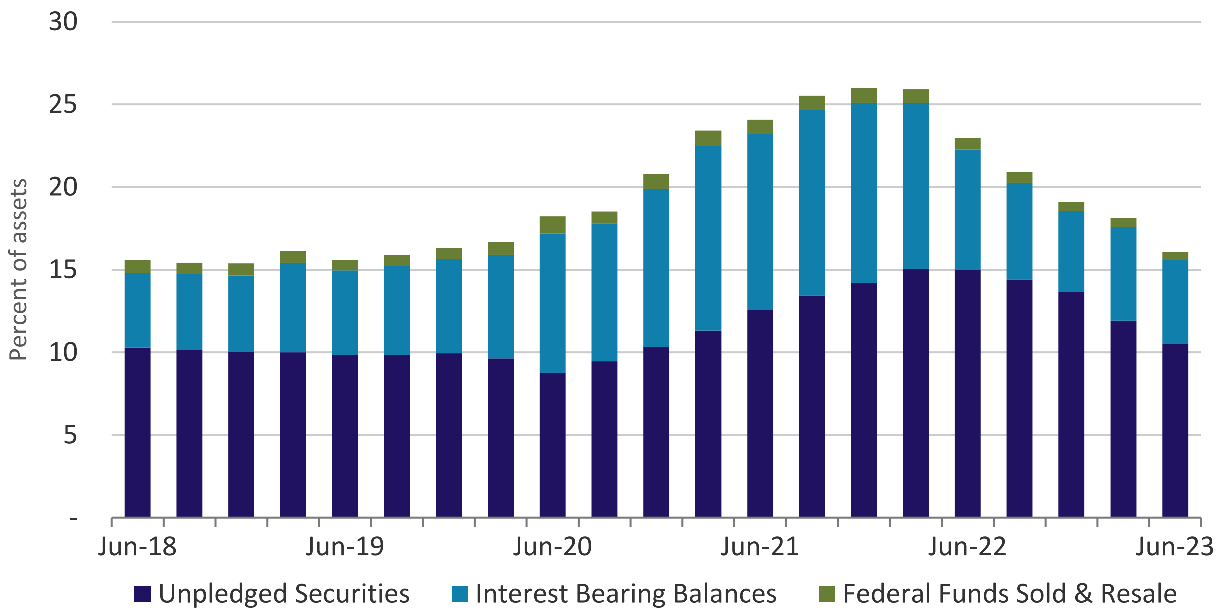
Community Banking BULLETIN: Highlight

Providing insights on community banking

Liquid Assets Declining From Pandemic Highs

The level of assets generally considered highly liquid has seen a significant decline as on-balance sheet liquidity has been used to fund loan growth and deposit runoff over the prior year.

Liquid Asset Levels



Source: Reports of Condition and Income

- In recent quarters, banks have decreased holdings of liquid assets, defined here as unpledged investment securities, interest-bearing bank balances, federal funds sold, and securities purchased under agreements to resell. Across community banking organizations[1] (CBOs), liquid assets decreased to 16 percent of total assets as of June 30, 2023, down from a peak of 26 percent at year-end 2021.
- Throughout 2020 and 2021, influxes of pandemic-induced deposits were placed in liquid assets as loan growth (outside of Paycheck Protection Program loans) stalled. Subsequently, in 2022 and 2023, liquid assets have been used to fund outsized loan growth and deposit runoff. While some banks added more cash items in the first quarter of 2023, likely out of caution due to market turmoil, these accounts again declined in the second quarter.
- The liquidity of securities, or the ability to liquidate securities at a reasonable cost, is further impacted by high levels of unrealized losses in investment portfolios.[2] Additionally, on-balance sheet liquidity is hindered by increased pledging of securities, with almost 50 percent of securities now pledged for the purpose of collateralized borrowing options.

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

[1] Community banking organizations are defined as having less than $10 billion in total assets

[2] See [Highlight: Unrealized losses mount across securities portfolios - Federal Reserve Bank of Kansas City (kansascityfed.org)]