

# FSOC

Financial Stability Oversight Council



## 2025 ANNUAL REPORT

# Financial Stability Oversight Council

The Financial Stability Oversight Council (Council) was established by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and is charged with three purposes:

1. To identify risks to the financial stability of the United States (U.S.) that could arise from the material financial distress or failure, or ongoing activities, of large, interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace.
2. To promote market discipline by eliminating expectations on the part of shareholders, creditors, and counterparties of such companies that the U.S. government will shield them from losses in the event of failure.
3. To respond to emerging threats to the stability of the U.S. financial system.

Pursuant to the Dodd-Frank Act, the Council consists of ten voting members and five nonvoting members and brings together the expertise of federal financial regulators, state regulators, and an insurance expert appointed by the President.

The voting members are:

- the Secretary of the Treasury, who serves as the Chairperson of the Council;
- the Chair of the Board of Governors of the Federal Reserve System;
- the Comptroller of the Currency;
- the Director of the Consumer Financial Protection Bureau;
- the Chairman of the Securities and Exchange Commission;
- the Chairman of the Federal Deposit Insurance Corporation;
- the Chairman of the Commodity Futures Trading Commission;
- the Director of the Federal Housing Finance Agency;
- the Chairman of the National Credit Union Administration; and
- an independent member having insurance expertise who is appointed by the President and confirmed by the Senate for a six-year term.

The nonvoting members, who serve in an advisory capacity, are:

- the Director of the Office of Financial Research;
- the Director of the Federal Insurance Office;
- a state insurance commissioner designated by the state insurance commissioners;
- a state banking supervisor designated by the state banking supervisors; and
- a state securities commissioner (or officer performing like functions) designated by the state securities commissioners.

The state insurance commissioner, state banking supervisor, and state securities commissioner serve two-year terms.

## **Statutory Requirements for the Annual Report**

Section 112(a)(2)(N) of the Dodd-Frank Act requires that the Council's annual report address the following:

1. the activities of the Council;
2. significant financial market and regulatory developments, including insurance and accounting regulations and standards, along with an assessment of those developments on the stability of the financial system;
3. potential emerging threats to the financial stability of the United States;
4. all determinations made under Section 113 or Title VIII and the basis for such determinations;
5. all recommendations made under Section 119 and the result of such recommendations; and
6. recommendations—
  - a. to enhance the integrity, efficiency, competitiveness, and stability of United States financial markets;
  - b. to promote market discipline; and
  - c. to maintain investor confidence.

## **Approval of the Annual Report**

This annual report was approved by the voting members of the Council on December 11, 2025.

Abbreviations for Council member agencies and member agency offices:

- Department of the Treasury (Treasury)
- Board of Governors of the Federal Reserve System (Federal Reserve)
- Office of the Comptroller of the Currency (OCC)
- Consumer Financial Protection Bureau (CFPB)
- Securities and Exchange Commission (SEC)
- Federal Deposit Insurance Corporation (FDIC)
- Commodity Futures Trading Commission (CFTC)
- Federal Housing Finance Agency (FHFA)
- National Credit Union Administration (NCUA)
- Office of Financial Research (OFR)
- Federal Insurance Office (FIO)

# Letter from the Chairperson

Title I of the Dodd-Frank Act created the Financial Stability Oversight Council (Council) and gave it the purposes of identifying risks to the financial stability of the United States, promoting market discipline, and responding to emerging threats to the stability of the U.S. financial system. Notably, the Act did not define the term “financial stability.”

Historically, financial stability analysis has centered on identifying vulnerabilities in financial institutions or markets that could, in certain adverse conditions, result in disruption in the provision of credit or liquidity or in other critical financial services such as payments, thereby leading to material stress and significant losses in the broader financial system. But monitoring and addressing these vulnerabilities, although important, is not sufficient for safeguarding financial stability. Financial stability also requires and is interdependent with sustainable long-term economic growth and economic security.

**Economic growth** is critical to financial stability. When economic output and incomes rise, debt burdens shrink relative to earnings, loan performance improves, and tax revenues strengthen the government’s fiscal position. Yet prophylactic financial regulatory and supervisory policies generally do not account for their overall impact on economic growth. Most often, any cost-benefit analysis of a new regulation assesses the rule’s costs in isolation. The cumulative burdens of regulatory and supervisory regimes, and the interactions among individual rules, are rarely considered.

The Council has a statutory duty to monitor financial regulatory proposals and developments and to make recommendations to enhance the integrity, efficiency, and competitiveness—as well as the stability—of U.S. financial markets. To fulfill that obligation, the Council will work with and support member agencies in considering whether aspects of the U.S. financial regulatory framework impose undue burdens and negatively impact economic growth, thereby undermining financial stability.

**Economic security** similarly undergirds financial stability. In the national security context, the term “economic security” is defined in U.S. law to mean the condition of having secure and resilient domestic production capacity, combined with reliable access to the global resources necessary to maintain an acceptable standard of living and to protect core national values.<sup>1</sup>

Economic security is also core to financial stability. The fallout from the loss of the capacity to maintain the nation’s standard of living can contribute to financial instability. Conversely, economic security requires that the U.S. financial system reliably provide the resources necessary to enable the real economy to support domestic production capacity, Americans’ standard of living, and our core national values. The concept of economic security should therefore be mapped onto the Council’s paradigm for assessing U.S. financial stability. Economic security and financial stability can be bolstered by technologies that strengthen the financial system’s defenses against malicious attacks and by financial regulation that appropriately incentivizes the flow of credit to strategic sectors.

This focus on economic growth and security will be reflected in the Council’s future approach to identifying priorities, evaluating risks, and recommending regulatory or supervisory changes. To that end, in 2026, the Council’s priorities will be operationalized through interagency staff committees and working groups, which will reflect the economic growth and economic security prisms of financial stability.

First, the Council has formed a new market resilience working group which will focus on Treasury, short-term wholesale funding, equity, and credit markets. Market-based credit and liquidity intermediation is a key source of strength for the U.S. economy. Markets supply capital that is a crucial supplement to bank lending, and their smooth functioning contributes to price discovery and efficiency. Businesses

and individuals depend on capital markets to fund their businesses and save for the future. Resilient markets are therefore important for economic growth and economic security and for financial stability. This working group will monitor for vulnerabilities that could affect financial stability, and it will also consider whether regulation has distorted or imposed undue costs on these critical markets in ways that could negatively impact economic growth and economic security.

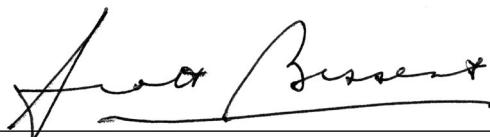
Second, the Council has formed a new household resilience working group that will focus on American households' financial condition. Financially resilient households can better withstand shocks, maintain essential consumption, and avoid costly debt cycles. Strong household balance sheets buoy Main Street during downturns in the business cycle. With savings buffers, diverse income streams, and insurance, households can recover faster from job losses, illness, disasters, or financial shocks. In addition, healthy household financials are critical for a mobile and entrepreneurial workforce, as well as higher investment rates and small business creation—all elements that are critical for long-term and sustainable economic growth. Therefore, the Council will monitor household financial resilience and consider early-warning indicators of potential stress in household balance sheets. The Council will also assess key trends affecting households' financial resilience, including those related to household borrowing and credit access and developments in the housing and mortgage markets.

Third, a new artificial intelligence (AI) working group will explore opportunities for AI to promote the resilience of the financial system while also monitoring for potential risks to financial stability that might be posed by the adoption of AI. The working group will identify potential high-value AI use cases that Council member agencies can adapt to streamline their own approaches to AI integration, with the aim of improving the efficiency and efficacy of the agencies' regulation and supervision. The working group will also provide a forum for public-private dialogue to identify regulatory impediments to the responsible adoption of AI technology by entities in the financial services sector.

Fourth, the Council will focus on crisis preparedness. Through this new workstream, the Council will support interagency efforts to prepare for cyberattacks or disruptions at critical service providers, including through the potential acquisition of quantum technology by threat actors. The Council's work will also assess potential threats to financial stability from other kinds of technological advancements and geopolitical risks.

The Council will continue its ongoing monitoring and coordination efforts through the Systemic Risk Committee (SRC) and the Financial Market Utilities and Payment, Clearing, and Settlement Activities (FMU) Committee. The SRC will remain a forum for staff of member agencies to convene, share information on recent financial-sector events, and monitor developments in financial markets. The FMU Committee will also continue to review the designations of systemically important financial market utilities and monitor the entry of new financial market utilities.

I am confident that by forging this new path, the Council will maintain its vigilance for material risks to financial stability while developing a better understanding of how the imperative for long-term and sustainable economic growth and economic security should factor into financial stability policy and analysis.



**Scott K. H. Bessent**

Secretary of the Treasury

Chairperson, Financial Stability Oversight Council

# Table of Contents

<b>Section 1. Member Statement .....</b>	<b>8</b>
<b>Section 2. Executive Summary .....</b>	<b>9</b>
2.1 Key Areas of Focus and Recommendations .....	9
2.2 Significant Market Developments to Monitor .....	11
<b>Section 3. Key Areas of Focus and Recommendations .....</b>	<b>12</b>
3.1 Bolstering Treasury Market Resilience .....	12
3.2 Addressing Cyber Risk and Navigating an Evolving Threat Landscape .....	16
3.3 Enhancing Supervisory and Regulatory Frameworks for Depository Institutions.....	18
3.4 Harnessing Artificial Intelligence to Promote Financial Stability .....	21
<b>Section 4. Significant Market Developments to Monitor.....</b>	<b>25</b>
4.1 Financial Markets .....	25
4.1.1 Short-Term Funding Markets .....	25
4.1.2 Commercial Real Estate .....	29
4.1.3 Corporate Credit .....	32
4.1.4 Household Credit.....	35
4.1.5 Residential Real Estate.....	38
4.1.6 Digital Assets .....	41
4.2 Financial Institutions .....	43
4.2.1 Depository Institutions .....	43
4.2.2 Investment Funds.....	47
4.2.3 Central Counterparties.....	51
4.2.4 Insurers .....	55
<b>Section 5. Council Activities and Regulatory Developments .....</b>	<b>58</b>
5.1 Council Activities .....	58
5.1.1 Risk Monitoring and Regulatory Coordination.....	58
5.1.2 Determinations Regarding Nonbank Financial Companies .....	58
5.1.3 Operations of the Council .....	58

5.2 Safety and Soundness .....	59
5.2.1 Enhanced Capital and Prudential Standards and Supervision.....	59
5.2.2 Dodd-Frank Act Stress Tests .....	60
5.2.3 Resolution Planning and Orderly Liquidation .....	61
5.2.4 Insurance .....	61
5.3 Financial Infrastructure, Markets, and Oversight .....	62
5.3.1 Digital Assets, Payment Systems, and Technological Innovation .....	62
5.3.2 Derivatives, Swap Data Repositories, Regulated Trading Platforms, Central Counterparties, and Financial Market Utilities.....	63
5.3.3 Securities and Asset Management.....	64
5.3.4 Accounting Standards .....	64
5.3.5 Bank Secrecy Act/Anti-Money Laundering Regulatory Reform .....	65
5.4 Mortgages and Housing Finance.....	67
<b>Section 6. Abbreviations .....</b>	<b>68</b>
<b>Section 7. Glossary .....</b>	<b>72</b>
<b>Section 8. List of Charts.....</b>	<b>77</b>
<b>Section 9. Endnotes.....</b>	<b>79</b>

# Section 1. Member Statement

**The Honorable Mike Johnson**  
Speaker of the House  
United States House of Representatives

**The Honorable Hakeem Jeffries**  
Democratic Leader  
United States House of Representatives

**The Honorable JD Vance**  
President of the Senate  
United States Senate

**The Honorable John Thune**  
Majority Leader  
United States Senate

**The Honorable Charles E. Schumer**  
Democratic Leader  
United States Senate

In accordance with Section 112(b)(2) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, for the reasons outlined in the annual report, I believe that additional actions, as described below, should be taken to ensure financial stability and to mitigate systemic risk that would negatively affect the economy: the issues and recommendations set forth in the Council's annual report should be fully addressed; the Council should continue to build its systems and processes for monitoring and responding to emerging threats to the stability of the U.S. financial system, including those described in the Council's annual report; the Council and its member agencies should continue to implement the laws they administer, including those established by, and amended by, the Dodd-Frank Act, through efficient and effective measures; and the Council and its member agencies should exercise their respective authorities for oversight of financial firms and markets so that the private sector employs sound financial risk management practices to mitigate potential risks to the financial stability of the United States.

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**Scott K. H. Bessent**  
Secretary of the Treasury  
Chairperson, Financial Stability Oversight Council

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**Jonathan V. Gould**  
Comptroller of the Currency  
Office of the Comptroller of the Currency

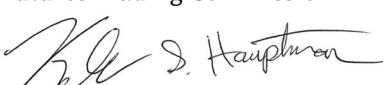
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**Paul S. Atkins**  
Chairman  
Securities and Exchange Commission

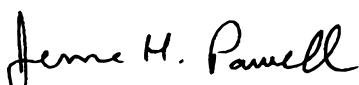
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**Caroline D. Pham**  
Acting Chairman  
Commodity Futures Trading Commission

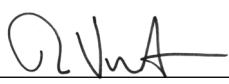
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**Kyle S. Hauptman**  
Chairman  
National Credit Union Administration

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**Jerome H. Powell**  
Chair  
Board of Governors of the Federal Reserve System

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**Russell Vought**  
Acting Director  
Consumer Financial Protection Bureau

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**Travis Hill**  
Acting Chairman  
Federal Deposit Insurance Corporation

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**William J. Pulte**  
Director  
Federal Housing Finance Agency

# Section 2. Executive Summary

Congress established the Council to identify risks to U.S. financial stability, promote market discipline, and respond to emerging threats to the stability of the U.S. financial system. To that end, the Council reports to Congress each year on potential and emerging threats to financial stability and makes recommendations to enhance the integrity, efficiency, competitiveness, and stability of domestic financial markets; to promote market discipline; and to maintain investor confidence. This report presents the Council's assessment of the most salient financial stability issues, provides the Council's recommendations to address these issues, and summarizes the activities of the Council and member agencies to address current and potential threats to U.S. financial stability.

U.S. financial markets and institutions performed well in 2025, supporting the smooth provision of credit to businesses and households and effectively facilitating asset price discovery. Core markets and institutions, including critical short-term funding and Treasury markets, and payment, clearing, and settlement systems, remained operational and resilient in the face of a short-lived bout of market volatility in early April 2025. Although this volatility caused a temporary but significant tightening in financial conditions, asset prices have since rebounded and now stand elevated relative to underlying fundamentals in several asset classes, reflecting strong investor risk appetite.

Aggregate measures of household and corporate debt remained stable over the past year, and fundamentals in both sectors have generally shown resilience. However, some emerging pockets of weakness among lower-rated corporate borrowers and within some segments of household credit bear monitoring. Conditions in the commercial real estate (CRE) market, which had deteriorated notably in the post-pandemic period, showed signs of stabilization in several property types.

Against this backdrop of a well-functioning financial system, important changes to financial

regulation, financial innovation and technology, and the risk landscape continue to present opportunities and risks to financial stability and command the careful attention of the Council. Given the wide set of issues relevant to financial stability, this year's report has been restructured to highlight the Council's priority areas of focus in Section 3, each of which are accompanied by actionable policy recommendations. Other sectors and markets where risks merit ongoing monitoring but do not have associated policy recommendations are detailed in Section 4. A summary of Sections 3 and 4 is below.

## 2.1 Key Areas of Focus and Recommendations

The Council has identified four key areas of focus in 2025. In order to improve the precision of this report, Section 3 discusses the most critical areas for Council members to focus on in the coming months. These recommendations include actions to bolster resilience in the U.S. Treasury market, mitigate increasingly sophisticated cyber threats, enhance our nation's bank supervisory and regulatory frameworks, and responsibly harness the potential of artificial intelligence (AI). Progressing on each of these four initiatives also would support financial stability by enhancing long-term economic growth and economic security.

### Bolstering Treasury Market Resilience

The U.S. Treasury market is the deepest and most liquid in the world with a unique role underpinning financial activity across domestic and global economies and performing numerous critical functions. Despite this irreplaceable role in the financial system, the Treasury market has experienced bouts of disruption in recent years, including in early April 2025 when liquidity conditions deteriorated alongside an abrupt increase in market volatility. While this episode was ultimately short-lived and the Treasury market continued to function throughout, the incident further underscored the importance of bolstering resilience to future shocks.

Council members have already implemented certain reforms aimed at enhancing market resilience; others remain in progress. The Council strongly supports the continued work of the Inter-Agency Working Group on Treasury Market Surveillance (IAWG). In further support of the IAWG, the Council encourages member agencies to utilize its new Market Resilience Working Group as a forum to monitor, analyze, and review resilience boosting initiatives in the Treasury market. Additionally, the Council supports the SEC in its efforts to implement a central clearing mandate for Treasuries. It also endorses banking agencies' recent finalization of a rule amending the enhanced supplementary leverage ratio (eSLR) and encourages banking agencies to consider other reforms that could remove undue impediments to Treasury market intermediation capacity. Finally, the Council recommends close monitoring of market developments, such as the potential entry of new Treasury central counterparties (CCPs) and implementation of the Guiding and Establishing National Innovation for U.S. Stablecoins Act (GENIUS Act), to better understand related impacts on Treasury market structure, functioning, and demand.

### **Addressing Cyber Risk and Navigating an Evolving Threat Landscape**

The cyber threat landscape continues to evolve rapidly with nation-state actors and sophisticated criminal groups continuing to target financial institutions and critical financial infrastructure. While cyber incidents have not had a major impact on financial stability thus far, they continue to pose significant risks due to the highly interconnected financial system, rapid advancements in technology that are enabling more sophisticated attacks, and limited substitutability of some critical services offered by third-party service providers. If successful, a significant cyber attack has the potential to disrupt operations, challenge access to liquidity, increase the likelihood of bank failures and market dysfunction, and erode confidence in the financial system, among other possible outcomes.

The public and private sectors remain highly focused on cyber threat detection and preparedness. Accordingly, financial institutions are managing operational and third-party risks, developing robust cyber incident response

programs, using and experimenting with novel technologies such as AI for cyber defense, and obtaining cyber insurance where appropriate. The public sector and the financial services sector are also increasing the use of tabletop exercises (TTXs) as an important tool for building readiness and resilience.

Going forward, the Council recommends that member agencies continue to expand joint monitoring and information sharing efforts among regulators and industry stakeholders and endorses the increased use of scenario-driven TTXs to help bolster preparedness for cyber incidents. To proactively expand cyber defense capabilities, the Council endorses increased public sector usage of AI and engagement with regulated private sector entities to encourage development of similar capabilities.

Cyber attacks that target third-party services are also an area of Council concern. Financial regulators have varying degrees of authority to supervise third-party service providers. Accordingly, the Council encourages federal banking regulators to continue coordination of third-party service provider examinations, expand collaborative outreach with state regulators, and identify additional ways to support information sharing among state and federal regulators. Further, the Council recommends that Congress pass legislation to ensure that FHFA has adequate examination and enforcement powers to manage the risks associated with services provided by third parties to its regulated entities.

Finally, the Council encourages public and financial services sector partners to consider the cryptographic risks of quantum computers and their impact on the future cyber risk landscape, and to take appropriate steps to facilitate the migration to quantum-resistant encryption technologies.

### **Enhancing Supervisory and Regulatory Frameworks for Depository Institutions**

An appropriately regulated and supervised banking system is critical to financial stability. Fifteen years after the wave of reforms made following the Global Financial Crisis (GFC), there is a recognition that while some reforms made the banking system more resilient to shocks, others have proven more costly than beneficial, and in some cases, have had unintended consequences.

A holistic review of regulation and supervision is now underway by banking agencies, with a focus on modernizing and simplifying the capital framework, tailoring supervision and regulation to the underlying risks, and revamping bank supervisory practices to refocus resources on material financial risks. The Council endorses proposals and actions taken by banking agencies and the NCUA in 2025 to enhance supervision and regulation of banks and credit unions and encourages consideration of new proposals and guidance to further modernize these frameworks, enhance transparency, reduce unnecessary regulatory burden, and better align regulatory treatment to avoid market distortions. Finally, the Council supports recent efforts by banking agencies to recalibrate regulatory and supervisory expectations, clearly define “unsafe or unsound practice” for supervisory and enforcement purposes, and reduce compliance costs for community banks.

### **Harnessing Artificial Intelligence to Promote Financial Stability**

While AI technologies have existed for decades, recent technological advances, including the development of Generative AI (GenAI) and agentic AI, have spurred a significant increase in adoption. Use cases in the public sector, the financial services sector, and the broader private sector have expanded quickly alongside these technological breakthroughs. Financial institutions are adopting AI for many purposes, such as lending, trading, insurance, and risk management. Similarly, financial regulatory bodies are exploring AI's use in supervision and regulation to improve productivity and organizational efficiency. Some agencies are beginning to use AI tools to develop early warning indicators, identify markets or firms with risk exposures, and analyze market sentiment.

Consistent with America’s AI Action Plan, the public sector is working to accelerate AI adoption throughout the federal government including by collaborating through the Chief Artificial Intelligence Officer (CAIO) Council.<sup>2</sup> Treasury has also appointed a CAIO and stood up the Treasury AI Transformation Office to drive AI adoption. Further, Treasury has engaged with private and public sector participants to explore use cases and promote responsible information sharing and best practices.

The Council recommends that member agencies use its Artificial Intelligence Working Group to explore opportunities for AI to promote the resilience of the financial system, while also monitoring for potential risks to financial stability that might be posed by the adoption of AI both within and outside the financial services sector. The working group will identify potential high-value AI use cases that Council member agencies can adapt to streamline their own approaches to AI adoption, with the aim of improving the efficiency and efficacy of the agencies’ supervision and regulation. The working group will also provide a forum for public-private dialogue to identify regulatory impediments to the responsible adoption of AI technology by financial institutions.

The Council also endorses continued cooperation by Treasury, the Financial and Banking Information Infrastructure Committee (FBICC), and the Financial Services Sector Coordinating Council (FSSCC) on these issues. Finally, it supports continued engagement with international counterparts concerned with the use of AI in financial services.

## **2.2 Significant Market Developments to Monitor**

Beyond the priority areas identified in Section 3, the Council continues to monitor important financial markets and institutions to remain well informed of significant developments and changes in the financial landscape. This monitoring work enables the Council to screen for potential risks to financial stability. Conditions in some sectors and markets have improved in 2025 in response to stabilizing trends in the CRE sector, improved performance of many depository institutions, and the passage of a much-needed statutory framework for payment stablecoins, among other factors. Other markets, such as residential real estate (RRE), have remained resilient in aggregate but continue to navigate challenges associated with current market dynamics, such as relatively high interest rates and house price affordability challenges. Going forward, the Council recommends continued monitoring of and information and analysis sharing concerning the markets and financial institutions discussed in Section 4.

# Section 3. Key Areas of Focus and Recommendations

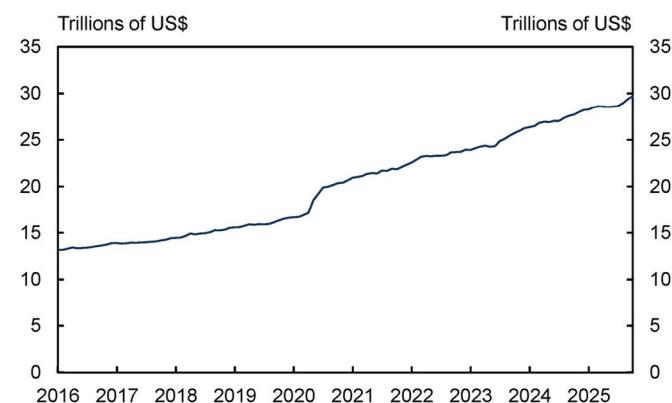
This section details four areas of focus related to financial stability that have been identified by the Council in 2025. At a high level, these include bolstering resilience in the critical U.S. Treasury market, navigating increasingly sophisticated cyber threats, enhancing our nation's bank supervisory and regulatory frameworks, and responsibly harnessing the power of AI. This set of issues represents the most critical areas for Council agencies to act on in the coming year. Policy recommendations are included for each.

## 3.1 Bolstering Treasury Market Resilience

### The Role of the Treasury Market

The Treasury market is the deepest and most liquid market in the world with an average daily trading volume of nearly \$1 trillion and over \$29 trillion outstanding (see **Figure 3.1.1**).<sup>3</sup> This large market plays several critical roles within the global financial system that include financing the U.S. federal government, facilitating the implementation of U.S. monetary policy, providing a safe and liquid asset for use as collateral, and providing accurate benchmark prices for use in securities valuation.

#### 3.1.1 U.S. Marketable Debt Held by the Public



Note: Data as of September 2025.

Source: Treasury.

Despite its size, liquidity, and preeminence, the Treasury market is not immune from periodic disruptions in market functioning. The most notable and disruptive event in the Treasury market over the past decade was the “dash-for-cash” episode at the beginning of the COVID-19 pandemic in 2020, though there have been other smaller episodes of reduced market functioning.<sup>4</sup> These episodic shocks, along with the associated effects on Treasury market liquidity and the broader financial system, highlight the importance of ongoing public sector efforts to increase the resilience of the Treasury market.

Bank regulations may have also impacted the market’s ability to absorb shocks. The value of U.S. Treasury securities outstanding has grown at a rate that has stressed the intermediation capacity of financial institutions. Specifically, bank-affiliated broker-dealer balance sheets had become more constrained due to certain post-crisis regulatory capital requirements, such as the eSLR. The eSLR requires the largest banking organizations to hold the same amount of capital against relatively low-risk assets, such as Treasury securities and repurchase agreements (repos), as required for high-risk assets.<sup>5</sup> At times, under the original calibration of the rule, this requirement had become a persistently binding constraint for large banks, incentivizing them to reduce engagement in lower-risk, lower-return activities, such as Treasury market intermediation.<sup>6</sup> Federal banking agencies recently finalized modifications to the eSLR calibration, with the aim of ensuring that the requirement serve as a backstop to risk-based requirements rather than as a constraint that is frequently binding over time.<sup>7</sup>

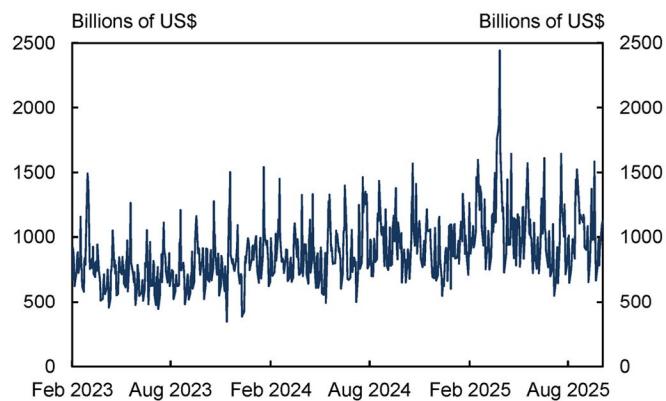
### Recent Market Developments

#### April Market Volatility

One of the more notable events in Treasury markets during 2025 occurred in early April. Liquidity conditions in the Treasury market declined as uncertainty associated with

international trade developments resulted in a spike in interest rate volatility. This spike caused many investors to reduce risk exposures in Treasuries. Over the course of the month, daily transaction volumes for Treasury securities reached record highs as market participants adjusted positions in response to evolving economic outlooks and to balance their risk exposures (see **Figure 3.1.2**). Liquidity metrics worsened as evidenced by wider bid-ask spreads, a decline in market depth, and an increase in the price impact of transactions. However, these metrics did not deteriorate to the same extent as during previous episodes of market stress, and they improved once levels of volatility reverted to more normal levels (see **Figure 3.1.3**).

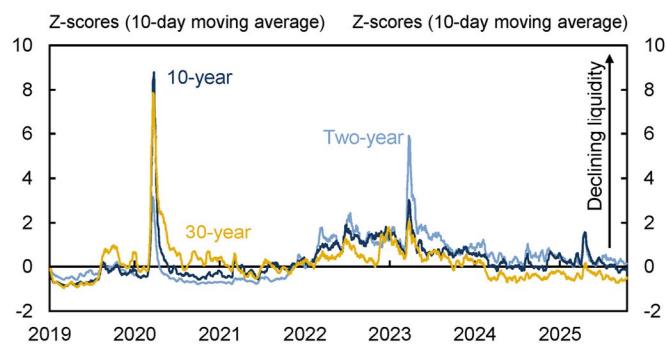
### 3.1.2 Total TRACE U.S. Treasury Daily Volume



Note: Data as of October 15, 2025.

Source: FINRA obtained through Bloomberg Finance L.P.

### 3.1.3 U.S. Treasury Market Liquidity Indexes



Notes: Data as of October 15, 2025. Index inputs are bid-ask, inverted depth, and price impact calculated for each security as the simple average of z-scores for each input. The two-year bid-ask/depth is reduced by half to account for the reductions in the minimum price increment. Increases in all indexes indicate a decline in liquidity, while decreases indicate improved liquidity.

Source: Treasury.

Despite the spike in volatility and decline in liquidity conditions in April, the Treasury market generally continued to function, in part because of stability in Treasury repo markets, which are key for Treasury security financing. During past periods of stress, market participants using a high degree of leverage were vulnerable to a spike in funding costs and, in some cases, unable to obtain or roll over financing from lenders. This forced institutions to exit their positions, selling off the Treasuries they held, which amplified market stress. This was particularly pronounced in March 2020, when leveraged investors unwound their cash-futures basis trade positions, which amplified stress in the Treasury market by adding to the broad selling of Treasury securities.<sup>8</sup> However, unlike March 2020, spreads between off-the-run and on-the-run Treasuries remained steady in April, and there was limited stress in the cash-futures basis trade.<sup>9</sup> Public sector measures implemented after March 2020, such as establishment of the Federal Reserve's Standing Repo Facility (SRF), which serves as a backstop to money markets to support monetary policy implementation and smooth market functioning, may have also played a role in enhancing market resilience.

One market segment that experienced greater disruption was swap spreads. Heading into April 2025, many leveraged participants, particularly hedge funds, were positioned to benefit from a widening of swap spreads due to an expectation that a potential easing of bank regulation would increase demand for Treasuries. This would potentially push Treasury yields lower relative to swap rates, causing the swap spread to widen and making the trade profitable. However, the unexpected market shock in early April and the resulting interest rate volatility forced these participants to unwind these positions. This unwind involved selling Treasuries, which contributed to upward pressure on Treasury yields and a notable decline in value relative to swaps during the period.

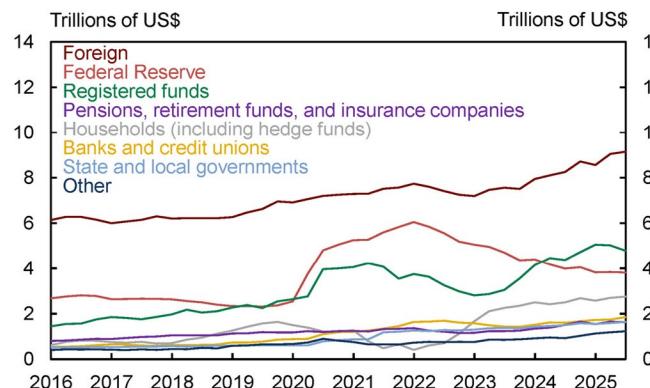
### Demand-Supply Dynamics and the Treasury Investor Base

Given the size of projected fiscal deficits, supply and demand dynamics in the Treasury market remained an important focus in 2025. Demand at Treasury auctions continued to be robust per a

variety of measures, such as bid-to-cover ratios and stop-out rates.<sup>10</sup> In addition, auction awards to primary dealers have continued to trend lower in 2025, suggesting significant end-user participation in Treasury auctions. When end users outbid dealers at Treasury auctions, dealers incur lower warehousing costs and use less of their balance sheet to underwrite auctions.

While demand for Treasuries has remained robust, over time, the composition of the investor base has shifted toward more price-sensitive investors such as hedge funds, which may have important implications for how Treasury markets respond to periods of heightened volatility (see **Figure 3.1.4**). This dynamic, which is in part a consequence of continued Treasury issuance to finance large deficits, has accelerated since mid-2022 when the Federal Open Market Committee (FOMC) began reducing its securities holdings; however, other private demand dynamics have contributed as well, as discussed below.

### 3.1.4 Holders of Treasury Securities



Notes: Data as of 2025:Q2. Registered funds include money market funds, mutual funds, closed-end funds, and exchange-traded funds.

Source: Federal Reserve Board.

Banks are an important source of Treasury demand that can be influenced by regulation. For example, the Liquidity Coverage Ratio requires large banks to hold high-quality liquid assets (HQLA), such as Treasuries, to cover net cash outflows during a 30-day stress period. Bank demand for Treasuries can also change due to differences in the growth rates of deposits and loans. Banks may allocate funds to Treasuries when deposit growth outstrips loan growth. Banks have become more attentive to interest rate risk and the price sensitivity of longer duration HQLA following the period of banking stress in March

2023, when rising interest rates created sizable unrealized losses for some banks. While bank holdings of Treasuries declined from mid-2022 through late-2023, holdings have increased over the last two years.

Foreign demand continues to provide significant support for the Treasury market. While there was market speculation on how international trade developments might impact foreign demand in the April period, foreign holdings of Treasury securities still reached record levels at over \$9 trillion as of July 2025. In recent years, growth in foreign demand has largely come from private investors while foreign public sector holdings of Treasury securities have been relatively flat. This change in foreign holdings composition could affect the overall dynamics of foreign demand in different interest rate environments. Historically, foreign demand has demonstrated some cyclicalities and can be affected by the level of U.S. policy rates due to related implications for the strength of the dollar and the relative level of yields. Further reductions in U.S. policy rates relative to other global policy rates could consequently reduce foreign demand for Treasury securities. Hedging costs also play a significant role in demand from foreign accounts as some foreign investors hedge their currency exposure to their U.S. Treasury holdings.

Asset managers that seek duration exposure to manage interest rate risk and efficiently achieve their clients' investment objectives often prefer to purchase Treasury futures in lieu of cash Treasuries. This strong demand for futures, which can be evidenced by the recent growth in asset managers' net futures positions, has contributed to a widening of spreads between futures and cash Treasuries.<sup>11</sup> The persistent imbalance in demand creates an opportunity for market participants, primarily hedge funds, to trade the cash-futures basis by selling futures and buying cash Treasuries. As a result, hedge funds engaged in highly leveraged basis trading have become an important source of Treasury demand but one that is relatively sensitive to interest rate volatility and funding market stability (see **Section 4.2.2**).

### Efforts to Bolster Treasury Market Resilience

The public sector remains focused on enhancing Treasury market resilience to ensure that it

continues to be the deepest and most liquid market in the world. In recent years, this work has been coordinated by the IAWG, which includes staff from Treasury, the Federal Reserve Board, Federal Reserve Bank of New York (FRBNY), SEC, and CFTC. As of 2025, IAWG member agencies have implemented several key reforms with others currently in progress.

#### *Buyback Program*

Launched in 2024, the Treasury buyback program provides liquidity support and seeks to improve Treasury's cash management.<sup>12</sup> The buyback program has been broadly successful in meeting Treasury's stated goals over its first year. In 2025, Treasury announced a review of ways to further enhance the program's efficacy and subsequently implemented several initial enhancements: (1) doubling the frequency of long-end nominal coupon liquidity support buybacks and increasing the aggregate size of liquidity support buybacks, (2) increasing the size of cash management buybacks, and (3) permitting a limited number of additional counterparties beyond primary dealers to directly access buyback operations beginning in the first half of 2026.

#### *Standing Repo Facility*

The Federal Reserve in 2021 introduced the SRF as a backstop to money markets to support the effective implementation and transmission of monetary policy and smooth market functioning.<sup>13</sup> In June 2025, the FRBNY began offering a daily morning operation to complement its existing afternoon operation, which would allow for settlement earlier in the day and better meet the intraday financing needs of some SRF counterparties.

#### *Changes to the Enhanced Supplementary Leverage Ratio*

In November 2025, federal banking regulators finalized modifications to the eSLR to reduce the likelihood that this requirement would be a regularly binding constraint (rather than a backstop to risk-based measures) and, by extension, limit the disincentive for banks to engage in low-risk activities, such as Treasury market intermediation.

#### *Non-Centrally Cleared Bilateral Repo Data Collection*

In May 2024, the OFR published a final rule for a non-centrally cleared bilateral repo (NCCBR) data collection program.<sup>14</sup> NCCBR was the largest remaining data gap in the public sector's understanding of repo market dynamics, which this data collection works to address. The OFR final rule identified two categories of relevant financial companies by the type and scale of their activity. Category I covered reporters began reporting in December 2024, while Category II covered reporters began reporting in July 2025.<sup>15</sup>

#### *Central Clearing*

In December 2023, the SEC adopted standards for central clearing of U.S. Treasury securities to expand central clearing of eligible Treasury securities and repo transactions. In February 2025, the SEC extended the compliance dates for its rule by one year to permit sufficient time for the market to properly implement the operational and risk management changes necessary to comply with this rule.<sup>16</sup> The SEC staff also has issued guidance designed to respond to questions raised by market participants regarding implementation of the rule, and continue to engage with market participants to discuss additional issues related to implementation. Increased central clearing resulting from the rule should improve risk management at CCPs and help improve dealer capacity, resulting in a more resilient Treasury market.

#### **Recommendations**

The Council supports the work of the IAWG and recommends that member agencies continue studying and implementing policies to improve the resilience of the Treasury market.

The Council recommends that member agencies also use its new Market Resilience Working Group as an interagency forum to supplement and reinforce the IAWG's recommendations.

The Council supports the SEC as it works towards implementation of the central clearing mandate for Treasuries.

The Council endorses monitoring, through the Financial Market Utilities and Payment, Clearing, and Settlement Activities (FMU) Committee, of the risks and opportunities created by new CCPs entering the Treasury market.

The Council endorses the federal banking agencies' recent finalization of a rule amending the eSLR and recommends that these agencies continue to evaluate banking sector reforms that would remove unduly burdensome regulatory or supervisory impediments to banks' Treasury market intermediation.

The Council supports full implementation of the GENIUS Act and monitoring the related growth of payment stablecoins as a growing source of demand for Treasuries.

### **3.2 Addressing Cyber Risk and Navigating an Evolving Threat Landscape**

#### **Cyber Incidents and Financial Stability Implications**

The cyber threat landscape is evolving rapidly, with nation-state actors and sophisticated criminal groups continuing to target financial institutions.<sup>17</sup> Financial institutions are lucrative targets because they manage substantial funds, hold sensitive customer data, and can be impacted by operational disruptions. Although cyber incidents have not resulted in a significant systemic event for the U.S. financial services sector to date, they could pose risks to financial stability given the high complexity and interconnectedness of global financial institutions and their systems. A cyber incident at a key financial institution, critical infrastructure or significant operation, or in an important market could propagate stress across the financial system. For example, incidents involving services provided by a significant third-party service provider could affect multiple financial institutions and their customers, particularly where there is limited substitutability for the affected services. The potential consequences of cyber incidents include large-scale service disruptions, challenges with accessing liquidity, compromised data, and a loss of confidence in institutions, markets, and the global financial system.<sup>18</sup>

Preparedness for the possibility of destabilizing cyber incidents continues to be a high priority for both the public and private sectors. Operational resilience is key for financial stability and should be continuously tested, evaluated, and strengthened to keep pace with evolving risks.

To enhance operational resilience, financial institutions are managing operational and third-party risks; developing robust cyber incident response programs; experimenting with novel technologies, such as AI, for cyber defense and fraud detection; and obtaining cyber insurance. Cyber insurance generally covers cyber incidents, including ransomware attacks, that impact an individual organization but not catastrophic cyber incidents with potential systemic impacts. The public and financial services sectors also find that exercises, such as TTXs, are an important tool for building readiness and resilience.

#### **Evolving Nation-State Threats and Cybercriminal Campaigns**

The operational resilience of the financial services sector also depends on the reliability of other critical infrastructure sectors, which nation-state actors are targeting. Geopolitical threats are likely to continue to manifest through cyber attacks that threaten national and economic security. For example, U.S. government agencies assess that the People's Republic of China (PRC)'s state-sponsored cyber actors are seeking to pre-position themselves on information technology (IT) networks.<sup>19</sup> Among other possible motives, this action may be in preparation for disruptive or destructive cyber attacks against U.S. critical infrastructure in the event of a major conflict with the United States. Similarly, PRC-affiliated threat actors' unauthorized access to commercial telecommunications infrastructure raises confidentiality, integrity, and availability concerns for all network users, including the financial services sector.<sup>20</sup>

Other prominent methods of cyber attacks include distributed denial-of-service (DDoS) attacks, ransomware and extortion, IT worker scams, digital asset theft, and cyber-enabled fraud. Risks posed by DDoS attacks are rising, where attackers disrupt operations by overwhelming targeted systems with malicious traffic and sometimes disable firms' abilities to communicate with customers, undermining consumer confidence.<sup>21</sup> While the average ransomware payment has decreased and fewer victims are paying ransoms, the number of ransomware incidents continues to rise across sectors.<sup>22</sup> The Democratic People's Republic of Korea (DPRK) has engaged in a yearslong campaign to generate revenue by

securing agents IT jobs under false identities and propagating cyber attacks. These efforts evade sanctions, pose operational risks to targeted firms, and, in some cases, introduce malware into company networks to exfiltrate proprietary and sensitive data.<sup>23</sup> Further, digital asset theft has been highlighted by the DPRK stealing \$1.5 billion from the digital asset exchange ByBit in 2025.<sup>24</sup> Lastly, transnational groups and other criminals have exploited social engineering and used other techniques to carry out cyber-enabled fraud activities, with total reported losses of \$13.7 billion last year.<sup>25</sup>

In recent years, threat actors have been empowered by advancements in technologies such as AI, enabling attacks that are more sophisticated, scalable, adaptive, and difficult to detect. GenAI can lower the barrier to entry for cyber attackers and be used to enhance social engineering and convincingly mimic trusted individuals through image, voice, and video generation. Adversaries are also exploiting AI to develop malicious code, craft personalized phishing messages, create fraudulent websites for investment scams, and deploy chatbots to lure victims into clicking malicious links. Data poisoning and integrity attacks can also occur at any stage of AI development and the data supply chain.

Looking ahead, advances in quantum computing present a potential threat to widely used encryption methods, including for digital assets, as quantum computers capable of bypassing current cryptographic algorithms could emerge in the next five to ten years. Additionally, adversaries are likely already conducting “harvest now, decrypt later” attacks in which they steal encrypted data today with the intent to decrypt it using quantum capabilities in the future. Migration to post-quantum cryptography may require five to fifteen years to complete, requiring early planning and upfront investment.<sup>26</sup>

### **Use of Third-Party Service Providers Can Intersect with Cyber Risks**

Third parties can provide a range of services and benefits to financial institutions, such as generating revenues, reducing costs, improving operational resilience, and enabling the faster development and scaling of a firm’s products and

services. Financial institutions are increasingly using third-party services for a range of use cases, including cloud-based services and AI. While financial institutions’ relationships with service providers provide significant new opportunities and lower the barrier to entry for new innovative technologies, such relationships may also present elevated risks if not appropriately managed. These risks can manifest in part because reliance on a third party may reduce an institution’s access to and its direct control and oversight of its data or systems.

Community banks and small firms are also increasingly reliant on third parties alongside their larger peers. However, they have less negotiating power to obtain certain contractual rights and fewer resources to conduct due diligence and monitor the third-party service provider’s practices. Thus, as service providers play a larger role in supporting important functions of financial institutions, supervisory agencies should have the necessary tools to oversee the related safety and soundness risks.

### **AI Technologies Can Help Counter Increasingly Sophisticated Attacks**

AI is emerging as a useful defense instrument against cyber attacks by reducing incident response times and costs, providing more accurate and efficient threat management, enabling faster decision-making, and enhancing system resilience. AI can enable real-time anomaly detection, rapid threat identification, and automated risk containment. In the financial services sector, AI can enhance resilience by monitoring transactions and network activity for suspicious behavior and provides government agencies with capabilities to detect risks at scale.<sup>27</sup> Treasury’s Office of Cybersecurity and Critical Infrastructure Protection (OCCIP), in collaboration with FBICC and the FSSCC, is partnering with the financial services sector to better understand AI’s role in shaping the sector’s cyber resilience and addressing challenges to adoption in the newly established AI Executive Oversight Group.<sup>28</sup>

### **Tabletop Exercises Help Defend Against Cyber Threats**

In addition to managing risks and leveraging AI, the public and financial services sectors continue to use TTXs for readiness and resilience. TTXs

provide financial institutions, regulators, and other stakeholders with a safe environment to test decision making, coordination, and response to complex scenarios that could impact the sector. For instance, TTXs can explore actions taken by individual firms that could affect other firms, such as decisions to disconnect or reconnect a firm's systems after a cyber attack.<sup>29</sup> By simulating both established and emerging threats, TTXs allow organizations to identify gaps, refine playbooks, and strengthen protocols before a real crisis occurs. TTXs also provide an opportunity to prepare for emerging risks like quantum-enabled threats and encourage creative dialogue on mitigation and forward-leaning transition strategies. Importantly, these exercises promote cross-sector collaboration and information sharing, both of which are essential to limiting contagion and preserving confidence during an incident.

Recent sector-wide TTXs have highlighted the importance of clear governance measures and early public communications to bolster public confidence. Building on the lessons of past exercises, future efforts should emphasize scenarios that cut across traditional boundaries, highlight systemic interdependencies, and stress test existing response capabilities. By integrating TTXs into ongoing risk management practices, the sector can better anticipate and respond to a wide range of threats, ultimately strengthening the resilience of financial institutions and preserving trust in the financial system.

## Recommendations

The Council recommends that member agencies continue to expand joint monitoring efforts, work with appropriate agencies and interagency groups (including FBIIC), and enhance information sharing among regulators and industry stakeholders (such as FSSCC), including to assess and mitigate cyber-related financial stability risks. The Council encourages the continued coordination of these engagements through Treasury's OCCIP.

To bolster cyber defense capabilities, the Council endorses increased public sector usage of advanced technology capabilities including AI. The public sector should also work with regulated entities to promote their development of such capabilities for cyber defense.

Given their proven utility and capacity for helping build a culture of dynamic resilience across the financial services sector, the Council endorses increased member agency usage of scenario-driven TTXs to assess public and private sector crisis preparedness for severe cyber incidents with potential systemic implications.

The Council encourages public and financial services sector partners to consider the risks to cryptography posed by quantum computers and to take the appropriate steps to facilitate the migration to quantum-resistant cryptography and transition towards greater cryptographic agility.

The Council endorses appropriate monitoring by federal banking regulators of the risks to the financial services sector from third-party service providers. To accomplish this, federal banking regulators are encouraged to continue coordination of third-party service provider examinations, expand collaborative outreach with state regulators, and identify additional ways to support information sharing among state and federal regulators. Further, the Council recommends that Congress pass legislation to ensure that FHFA has adequate examination and enforcement powers to manage the risks associated with services provided by third parties to its regulated entities.<sup>30</sup>

## 3.3 Enhancing Supervisory and Regulatory Frameworks for Depository Institutions

### The Importance of a Properly Calibrated Framework

An appropriately regulated and supervised banking system is critical to U.S. financial stability. Many of the regulatory reforms implemented in the wake of the GFC made the banking system more resilient to shocks. In hindsight, however, some reforms proved more costly than beneficial or necessary and have had unintended consequences, particularly for community banks. Since 2010, additional regulation and more stringent application of internationally agreed standards have been applied to U.S. banks.<sup>31</sup> As a result, 15 years after most post-GFC reforms were finalized, bank regulation has expanded into an increasingly complex and burdensome set of rules.

Going forward, the bank regulatory framework should be revisited to remove excessive impediments to economic growth, an effort that can, in turn, enhance financial stability. More specifically, reforms should be made that preserve the central role of the banking system in facilitating credit intermediation for American households and businesses while ensuring bank safety and soundness. Banking agencies should conduct cost-benefit analysis of significant regulations, considering any adverse effects on the efficient functioning of the economy.<sup>32</sup>

Recent experience also suggests that bank regulations can result in unintended consequences and economic distortions. One example of such a distortion in recent years is that as banking regulations have become more complex and costly, the share of credit originated by banks has declined. Lending has been driven out of the banking system, often to nonbank intermediaries.<sup>33</sup> The Council has previously acknowledged this dynamic in mortgage credit intermediation and made recommendations to mitigate the associated risks to financial stability.

Another unintended consequence has occurred as bank leverage ratios, which were long intended to serve as a backstop to banks' risk-based capital requirements, have increasingly and inadvertently become the persistently binding capital constraint for a rising number of banks. These requirements effectively disincentivize banks from engaging in important low-risk activities, such as Treasury market intermediation (see **Section 3.1**).<sup>34</sup>

In addition to the need to address unintended consequences, federal bank regulators have started to identify other specific issues in the current regulatory framework that may require action. These include appropriately tailoring regulatory standards and reducing compliance costs for community and midsized banks, removing overlapping requirements or unanticipated interactions between capital and liquidity requirements, and minimizing unexpected volatility in capital requirements associated with stress testing. Many of these issues and their proposed solutions are discussed in this section.

Finally, supervision has an important role in ensuring banks' safety and soundness, and strong

and clear supervisory practices are critical to financial stability. Indeed, focused supervision and appropriately calibrated regulation should be mutually reinforcing. However, in recent years, supervision shifted to look beyond its core focus on the material financial risks facing banks, expectations for larger banks were pushed to smaller, less complex community banks, and a lack of supervisory transparency may have resulted in moving goal posts and an overreliance on supervisory discretion.

As evidenced by the bank failures in spring 2023, unduly centering supervision on management and other governance matters can distract examiners and banks' risk managers from more direct risks to safety and soundness. The associated mission drift can also lend itself to political ends, such as excessive focus on climate risk and the effective debanking of certain industries. Collectively, this increases distraction and compliance costs while impeding responsible lending and risk-taking. Here too, banking agencies have begun to diagnose these problems and to propose meaningful solutions that will refocus supervisors on material financial risks while ensuring that supervision is appropriately tailored to the size and complexity of individual banking organizations.

## **Current, Planned, and Potential Reforms**

### *Capital and Other Regulatory Changes*

Bank regulators are prioritizing efforts to modernize the regulatory capital framework so that individual elements of the framework work together and are aligned with the latest data on the underlying credit, market, and operational risk of exposures. Federal banking agencies finalized amendments in November 2025 to modify the eSLR, as described above, to help ensure that leverage requirements serve as a backstop to risk-based capital requirements. Also in November, federal banking agencies proposed changes to the Community Bank Leverage Ratio (CBLR) to modify the ratio requirement and also the grace period applicable to institutions that temporarily fall out of compliance with the CBLR framework.<sup>35</sup> Earlier in 2025, the Federal Reserve proposed changes to its annual stress tests for large firms that are intended to reduce unexpected volatility in stress capital buffer requirements

applicable to large firms by averaging the results of the stress tests from two consecutive years. In addition, the proposal would provide banks with additional time to adjust to their new capital requirements by delaying the effective date of the stress capital buffer.<sup>36</sup> The Federal Reserve has published a proposal to consider more extensive changes to the stress testing process, to promote transparency and predictability.

Beyond leverage and stress testing requirements, bank regulators have also taken steps to consider reforms to additional requirements, including the Global Systemically Important Bank (G-SIB) surcharge and Basel III risk-based requirements. Finally, in November 2025 the FDIC finalized a rulemaking to raise and index certain regulatory standards to reflect inflation.<sup>37</sup> This will allow the FDIC to better differentiate and tailor a variety of regulatory requirements and their applicability to institutions over time.

#### *Changes to Supervision*

Besides improved tailoring of regulation, perhaps the single most important reform will be to refocus bank supervision on material financial risks. Federal banking agencies have also started implementing important changes to some areas of bank supervision in 2025 and have launched efforts to consider and propose deeper reforms. In a recent effort to squarely focus supervisory resources on material financial risks, in October 2025, the OCC and the FDIC issued a proposed rule to define “unsafe or unsound practices” for the purposes of supervision and enforcement.<sup>38</sup>

The Federal Reserve has also proposed and finalized changes to its Large Financial Institution (LFI) and Insurance Supervisory ratings framework to address the “well managed” status of these firms in a way that would more appropriately align the supervisory rating framework with the financial condition of firms subject to those rating systems.<sup>39</sup> To a similar end, the banking agencies have also announced that they will no longer consider reputational risk in supervisory examinations and will remove references to reputational risk from their supervisory materials.<sup>40</sup> To codify that policy, the OCC and the FDIC issued a proposed rule to preclude reputation risk as a basis for supervisory criticism or other regulatory action.<sup>41</sup> Finally,

the OCC, FDIC, and Federal Reserve have also announced their withdrawal of Principles for Climate-Related Financial Risk Management for Large Financial Institutions.<sup>42</sup>

Through a series of actions, the federal banking agencies have taken steps to clarify that banking organizations may engage in certain crypto-asset activities and provide products and services to customers engaged in crypto-asset related activities, consistent with safety and soundness and applicable laws and regulations. This has been communicated via the withdrawal of two joint statements issued in 2023 related to risks associated with banks’ crypto-asset activities and publication of a number of additional statements related to permissible engagements in crypto-asset activities.<sup>43</sup> As part of their actions, the agencies withdrew the expectation that banks notify and obtain a no-objection from their supervisors before engaging in certain new activities related to digital assets.

Additional efforts are underway to consider the appropriateness of the broader supervisory ratings framework for community and midsized banks, improve supervisory prioritization, enhance examiners’ compliance with supervisory policy, revisit the role of supervisory guidance, provide guidance on how banks may engage with innovative technologies, and more appropriately tailor supervisory activities and exams for smaller firms.<sup>44</sup> The OCC is in the process of revising examination approaches to community banks for certain areas like fair lending, capital, liquidity, the Community Reinvestment Act, and third-party risk management in an effort to adjust such approaches to reflect the low risks posed by community banking activities. Agencies have also taken action to speed up the adjudication of merger applications and decision making with regard to de novo charters to ensure that the banking system remains diverse in nature and dynamic in scope of activities.<sup>45</sup>

#### *Regulators to Focus on Similar Approaches for Credit Unions*

The NCUA, which supervises credit unions, works to protect the safety and soundness of the credit union system, including through identifying, monitoring and reducing risk to the National Credit Union Share Insurance Fund. In line with

banking agency efforts, the NCUA is working to streamline examination procedures, clarify credit union engagement with digital assets, explore ways to harness innovative technology, and improve supervisory approaches.<sup>46</sup> <sup>47</sup> The NCUA is also in the process of considering how best to reduce, streamline, or eliminate outdated or overly burdensome regulations and processes to ensure credit union competitiveness while prioritizing safety and soundness.

### **Recommendations**

The Council endorses current banking agency efforts to simplify and modernize regulatory capital standards. The Council encourages the banking agencies to ensure that these reforms do not put community banks and midsize banks at a competitive disadvantage.

The Council supports reforms to focus bank supervision on material financial risk and encourages the banking agencies to finalize a rule to define “unsafe or unsound practices,” among other reforms.

The Council also encourages banking agencies to quickly implement other proposed changes to supervisory frameworks and to act on further changes to promote supervisory efficiency, transparency, and fairness across institutions, with a focus on material financial risks.

The Council recommends that the regulatory agencies coordinate and take other appropriate action to avoid market distortions that could increase risks to financial stability by generally taking consistent approaches to the capital requirements and other regulation of similar risks across market participants, consistent with the business models and missions of their regulated entities.

The Council supports recent efforts of bank regulatory agencies to examine issues specific to community banks and encourages future proposals and modifications that would improve regulatory and supervisory transparency, efficiency, and simplicity for community banks.

The Council similarly supports the NCUA in its recent regulatory and supervisory reform efforts to streamline or eliminate overly burdensome regulations and processes to restore the focus

on mitigating the risks of a significant credit union failure. The Council encourages the NCUA to continue to focus its supervisory practices on material financial risks and preventing large institution failures, as well as preserving strong supervisory policies and procedures that reduce the likelihood of such a failure occurring.

The Council recommends that member agencies continue to proactively address any outstanding issues related to supervision and regulation of digital asset engagement by supervised institutions. This may include further issuance of clear expectations and/or guidance related to permissible activities (including holding digital assets on the balance sheet), digital asset custody, tokenization, holding stablecoin reserves as deposits, use of permissionless blockchains, anti-money laundering/countering the financing of terrorism (AML/CFT) obligations, third-party relationships, and the ability to participate in digital asset pilot programs.

The Council recommends that the federal bank regulatory agencies consider and prioritize practical measures to reduce regulatory burden identified through the Economic Growth and Regulatory Paperwork Reduction Act.<sup>48</sup>

## **3.4 Harnessing Artificial Intelligence to Promote Financial Stability**

### **AI Evolution**

AI has existed for decades, but its use in the financial services sector and the broader economy has accelerated in recent years through advancements in algorithms, big data, computational power, and data storage. While definitions of AI vary, the Council follows the definition of AI in Executive Order (EO) 14179 referencing 15 U.S.C. 9401(3): AI is a machine-based system that can, for a given set of human-defined objectives, make predictions, recommendations, or decisions influencing real or virtual environments.<sup>49</sup> Recent innovations with deep learning have facilitated more accurate predictions than traditional machine learning by using multi-layered neural networks to extract complex patterns from large data sets. Large language models (LLMs) have enabled more user-friendly interactions by processing and responding with human language rather than

code. GenAI technologies introduced in the last few years create human-like content, such as text, images, or videos. In the last year, agentic AI systems have been developed to pursue specific goals with some degree of autonomy based on real-time feedback from their environments. Reflecting the market's expectation that AI will become the dominant frontier technology, global corporate investment in AI reached \$252 billion in 2024, with the market projected to potentially grow rapidly over the next few years.<sup>50</sup> As with any new technology, careful attention will need to be paid to manage potential risks that could arise with the widespread adoption of AI.

### Potential Financial Stability Value and Risks of AI

AI usage has the potential to support economic growth by generating new insights, boosting operational efficiency, and improving risk management for the public and private sectors alike. Use of AI may also lower barriers to entry for entrepreneurs and support faster scaling for start-ups. Established firms are taking a deliberate approach to AI adoption, with CEOs expecting significant impacts to show in the three- to ten-year horizon.<sup>51</sup> AI usage has the potential to increase productivity, which is the foundation for economic growth. Estimates of gains in worker-level productivity with GenAI and LLMs are significant and range from 12 percent to 56 percent with potential gains in quality by 40 percent.<sup>52</sup> GenAI could qualify as a new general-purpose technology, permeating widely across sectors, continuously improving, and spawning positive loops of innovations.<sup>53</sup>

AI adoption has the potential to improve financial institutions' performance by enabling them to provide innovative services cheaper, faster, to a broader set of customers, and under varied economic conditions. Financial institutions are adopting AI for many use cases and functions, such as lending, trading, and insurance. In lending, AI can facilitate the use of alternative data, such as cash flow history, to evaluate a customer's creditworthiness, potentially expanding the availability of credit to customers with little or no credit history by community banks, credit unions, and financial technology (fintech) lenders. Use of such data may also improve accuracy, increase speed, and lower costs of credit underwriting.<sup>54</sup> In asset

management, AI can be used to prepare tailored financial advice and investment strategies, analyze market and sentiment developments, and stress test investment strategies under various market scenarios. AI can also be used to support automated trading, such as for order placement and execution, and to generate trade reports. Insurers are deploying AI across all stages of the insurance life cycle, such as to model catastrophes, improve pricing of policies to better reflect risks, and automate claims processing. Lastly, a variety of financial institutions use AI for risk management and regulatory compliance, such as to manage capital and liquidity, enhance cybersecurity, and detect fraud and illicit activities.<sup>55</sup>

Community banks can benefit from adopting AI to serve local communities, though they often lack the financial and other resources to develop, acquire, and scale AI tools compared to larger firms. For example, smaller firms may struggle to access the volume and diversity of data needed to develop robust AI applications, as well as attract, hire, and retain AI specialists. Smaller firms can acquire relevant expertise and other benefits from bank-fintech partnerships, though reliance on third-party AI solutions can also introduce dependencies, limitations, and risks as the firms do not completely control such tools.<sup>56</sup>

AI usage also has the potential to improve the effectiveness and efficiency of financial regulatory agencies. Agencies worldwide are experimenting with responsible use of AI in areas such as supervision and regulation, crisis readiness, and operational efficiency. In supervision, AI can be used to assess the compliance of firms' regulatory reporting submissions with regulatory requirements, monitor and surveil trades, or oversee payment systems. One Council member agency used machine learning to find potential errors in financial institutions' regulatory reporting submissions, which improved data quality, decreased the number of false positives, and significantly reduced manual review time. Another used AI for enhanced fraud detection processes, resulting in prevention and recovery of over \$4 billion in improper payments.<sup>57</sup> GenAI is also being used by foreign regulators for more advanced supervisory functions, such as risk horizon scanning, stress testing, and simulating aspects of bank failures. Relatedly,

in crisis readiness, some agencies are using AI tools to identify financial crises and forecast related metrics, develop early warning systems, and identify markets or firms with specific exposures.<sup>58</sup> AI can also be used to scan market developments, analyze sentiment, and produce economic forecasts based on public filings, news feeds, and social media. Lastly, agencies are exploring use of GenAI to improve operational efficiency and boost worker productivity, such as to store, process, and retrieve data like laws, legal cases, or reports; draft document summaries, emails, or software code; and prepare voice transcriptions.<sup>59</sup>

In addition to the benefits, widespread adoption of AI technology should also be monitored from a financial stability and economic security perspective to ensure that risks such as misuse by malicious actors, as well as national security, cyber, or other unanticipated risks, are well understood by member agencies and appropriately managed by financial institutions. For instance, financial institutions should continue to monitor and appropriately manage their exposures to AI-related companies due to valuations that reflect strong future earnings projections, and Council members should continue to monitor the potential impact of AI on financial institutions, the labor market, the broader macroeconomy, and household financial resilience.

### **Recent Public Sector Efforts to Harness AI's Benefits**

Recognizing the potential of AI, EO 14179 directed the formulation of an action plan to sustain and enhance America's global AI dominance.<sup>60</sup> America's AI Action Plan has three pillars: accelerate AI innovation, build American AI infrastructure, and lead in international AI diplomacy and security.<sup>61</sup> To accelerate AI innovation in the private sector, the AI Action Plan provides many recommendations. These recommendations include establishing regulatory sandboxes for firms to rapidly test AI tools; having the National Institute of Standards and Technology (NIST) convene stakeholders to accelerate the development of national standards for AI systems; and revising regulations that unnecessarily hinder AI adoption. The Office of Science and Technology Policy has issued a request for information to identify such regulations as well as other agency

actions to promote AI innovation.<sup>62</sup>

The plan also recommends accelerating AI adoption in government through actions like interagency collaboration via the CAIO Council; developing an AI procurement toolbox and facilitating transfer of advanced AI capabilities, use cases, and talent among agencies; and mandating appropriate training and access for employees whose work could benefit from access to frontier language models. OMB Memoranda M-25-21 and M-25-22 provide guidance to agencies on federal use of AI, such as identifying a CAIO to champion their agency's AI goals, developing a publicly available AI strategy, and implementing effective AI governance and minimum risk management practices.<sup>63</sup>

Treasury appointed its CAIO in June 2025 and began developing the Treasury AI Transformation Office to drive the adoption and implementation of AI across the agency. Treasury is committed to removing barriers to AI adoption not only within the agency but also across the broader financial services sector. To support this approach, Treasury has engaged with technology firms and financial institutions to understand the ways in which AI is being adopted while also exploring sector views. Treasury also meets regularly with other U.S. government agencies to share leading practices and explore cross-agency AI use cases. Finally, Treasury is supporting the U.S. G20 presidency to highlight U.S. innovation and leadership in AI, particularly in support of financial services, and demonstrate U.S. willingness to collaborate with global partners to expand access to these technologies.

### **Recommendations**

The Council recommends that member agencies use its Artificial Intelligence Working Group to explore opportunities for AI to promote the resilience of the financial system. The working group will also monitor potential risks to financial stability that might be posed by the adoption of AI both within and outside the financial services sector. The working group will identify potential high-value AI use cases that Council member agencies can adapt to streamline their own approaches to AI adoption, with the aim of improving the efficiency and efficacy of the agencies' supervision and regulation. The working

group will also provide a forum for public-private dialogue to identify regulatory impediments to the responsible adoption of AI technology by financial institutions.

The Council supports member agencies' efforts to foster responsible adoption of AI technology by regulated entities, including by demonstrating its potential to enhance the performance of the financial services sector and support economic growth.

The Council supports efforts led by Treasury, the FBIIC, and the FSSCC to continue cooperation in this area.

The Council supports continued engagement with international counterparts on the risks and benefits of AI in financial services as part of the global network.

# Section 4. Significant Market Developments to Monitor

This section highlights developments in select financial markets and financial institutions that are pertinent to U.S. competitiveness, efficiency, economic security, and financial stability. The section describes market developments and trends for each sector, including domestic and foreign regulation, and highlights issues that may have implications for financial stability, including any salient risks and transmission channels. The Council recommends continued monitoring of these markets and institutions both at member agencies and through its committees and working groups.

## 4.1 Financial Markets

### 4.1.1 Short-Term Funding Markets

Short-term funding markets provide financing for financial institutions, businesses, state and local governments, and the federal government. These markets are critical for implementing monetary policy and supporting financial market liquidity. They are also large, with the gross size of the repo market near \$12 trillion and approximately \$1.3 trillion of commercial paper outstanding.<sup>64</sup>

During both the GFC and in March 2020, short-term funding markets demonstrated vulnerability as shocks to the financial system were amplified by fragilities in these markets. Intermediaries in short-term funding markets perform significant liquidity and maturity transformation and can be vulnerable to runs during times of stress. The short-term nature of these markets can also subject the institutions that rely on them for funding to significant rollover risk based on market conditions. As such, it remains critical for financial stability that these markets function smoothly and that they are monitored for signs of disruption.

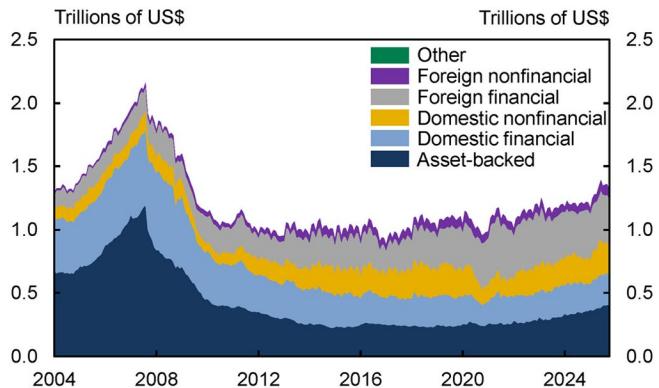
#### Commercial Paper

Commercial paper is a source of short-term funding used by both nonfinancial and financial firms. It is a short-term debt instrument with maturities not exceeding 270 days, but often around 30 days.<sup>65</sup> Investors often buy and hold

commercial paper to maturity because it is so short in term. Therefore, the volume of secondary market trading is low. Typically, investors looking to sell their commercial paper return it to the issuing dealer. When demand for liquidity rises sharply among commercial paper investors, as happened during the “dash for cash” in March 2020, investors may find issuing dealers less willing to buy back the paper. In turn, institutions that depend on the commercial paper market may be unable to obtain new funding as their short-term borrowings mature. Consequently, liquidity shortfalls in the commercial paper market can contribute to stress in other market sectors, cause dislocations in the real economy, and impact economic growth. Amid the market disruptions in March 2020, investor demand for commercial paper plummeted, particularly for terms beyond four days. As a result, with approval from the Treasury Secretary, the Federal Reserve established a Commercial Paper Funding Facility to ensure that firms were able to roll over their commercial paper. This episode illustrated the fragility in the commercial paper market, including the refinancing risks inherent in this market.

The amount of commercial paper outstanding has grown about 9 percent to nearly \$1.3 trillion over the past year but remains below levels observed in 2007 and 2008 (see **Figure 4.1.1.1**). Asset-backed commercial paper issuers and foreign financial firms are the most active issuers in the commercial paper market, accounting for 31 percent and 29 percent of commercial paper outstanding as of September 2025, respectively. Commercial paper spreads typically widen during market stress events, especially for lower-rated issuers (see **Figure 4.1.1.2**). Commercial paper spreads remained relatively stable over the past year, well below levels observed in the GFC and in March 2020.

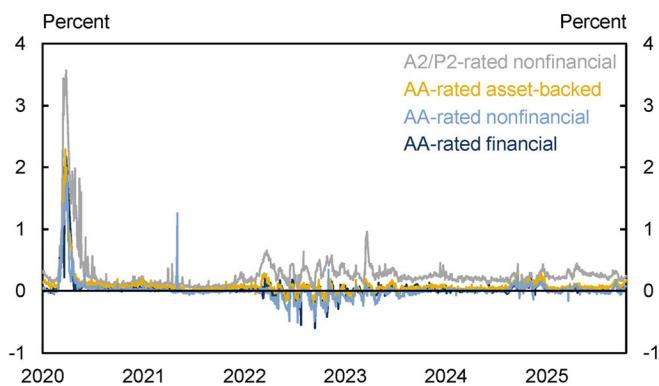
#### 4.1.1.1 Commercial Paper Outstanding by Issuer Type



Notes: Data as of September 2025. Not seasonally adjusted. "Domestic" includes commercial paper issued in the United States by entities with foreign parents.

Source: Federal Reserve Board obtained through Haver Analytics, Inc.

#### 4.1.1.2 One-Month Commercial Paper Interest Rate Spreads



Notes: Data as of October 15, 2025. Spread to one-month overnight index swap (OIS) rate.

Sources: Federal Reserve Board and London Stock Exchange Group. All sources obtained through Haver Analytics, Inc.

### Repo Markets

Repo markets are the primary source of collateralized short-term funding and play a critical role in Treasury market liquidity and monetary policy implementation. Additionally, overnight Treasury repo rates form the basis of the Secured Overnight Financing Rate (SOFR), a key interest rate benchmark used in many parts of the financial system.

Repos are a form of secured lending in which one firm sells a security to another firm with a simultaneous promise to buy the security back at a later date, often the next day, at a specified price. Recent estimates suggest that the gross size of the repo market stands near \$12 trillion.<sup>66</sup> The

repo market includes three segments: transactions centrally cleared through the Fixed Income Clearing Corporation (FICC); transactions not cleared through FICC but settled on the Bank of New York Mellon's tri-party settlement system; and NCCBR. New data collected by OFR suggests that NCCBR is the largest repo segment by a sizeable margin.

Large bank-affiliated securities dealers serve as significant intermediaries in repo markets by borrowing from cash lenders, such as money market funds (MMFs), and lending to entities that employ leverage, such as hedge funds. Dealers also borrow in repo markets to finance their own securities holdings, and bank affiliates of the larger dealers may lend cash into repo markets. As part of the Federal Reserve's monetary policy framework, Federal Reserve banks can engage in repo operations to implement monetary policy. The FRBNY also operates the Overnight Reverse Repo Facility (ON RRP) and the SRF. The ON RRP helps to place a floor for overnight interest rates by providing an investment alternative to private sector repo for MMFs and other eligible counterparties. The SRF helps to dampen market pressures that could lead the federal funds rate to exceed the Federal Reserve's target range by providing overnight repo financing to primary dealers and eligible depository institutions.

Stress in repo markets may propagate to broader financial markets given their size, their importance in providing financing to the cash Treasury and agency mortgage-backed security (MBS) markets, and the prominent roles played by LFIs.<sup>67</sup> Firms reliant on overnight or short-term repo financing may be vulnerable to funding shocks, particularly during times of market volatility, and they may transmit stress to other repo market participants and broader short-term funding markets. For example, net lenders in the repo market may pull back during periods of market stress to preserve cash to meet redemptions. At the same time, leveraged investors, such as hedge funds and mortgage real estate investment trusts, may face a sudden tightening in financing terms or be unable to roll over financing. Stress in repo markets in March 2020 highlighted how imbalances in the repo market can quickly transmit or amplify stress in the financial system. Repo markets remained resilient during the volatility in early April of this year, helping to moderate pressures experienced in the Treasury market at that time.

Treasury securities are the most common form of collateral used in repo transactions, accounting for approximately 70 percent of repo borrowing outstanding according to the FRBNY's primary dealer statistics.<sup>68</sup> Of the remaining 30 percent of repo borrowing outstanding, borrowing collateralized by agency debt and MBS accounts for approximately 20 percent, and borrowing collateralized by corporate bonds, equities, and other asset classes accounts for 10 percent. Roughly 80 percent of repo borrowing is on an overnight basis.

Cleared and tri-party repo trading volumes have grown in 2025 (see **Figure 4.1.1.3**). These increased volumes are consistent with rising hedge fund repo demand, which may reflect growth in the size of the cash-futures basis trade (see **Sections 3.1 and 4.2.2**). In general, repo market rates move closely with changes in the Federal Reserve's target range for its policy rate. As demand for repo financing has grown over the last year, benchmark rates on overnight Treasury repo—SOFR and the Tri-Party General Collateral Rate (TGCR)—have gradually risen relative to the rate on the Federal Reserve's ON RRP (see **Figure 4.1.4**).

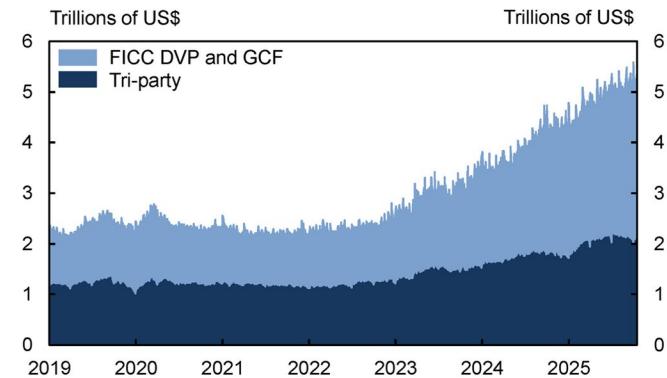
In December 2024, the OFR began an ongoing collection of NCCBR transaction-level data, which has for the first time provided regulators with timely insight into this market.<sup>69</sup> During periods of market volatility in early 2025, the OFR used the NCCBR data collection to help monitor markets for any indication of an unwind of highly leveraged positions that rely on financing in this market segment. The OFR communicated those findings to the regulatory community daily, which would have not been possible previously.

The data reveals that the NCCBR market segment averages about \$5 trillion in daily outstanding, making it the largest repo market segment by a considerable margin.<sup>70</sup> Hedge funds are active participants in the NCCBR market segment as they lend and borrow an average of nearly \$2 trillion a day, mostly transacting with broker-dealers and banks.

The NCCBR market segment differs from other repo market segments. For example, the OFR estimates that nearly one-third of NCCBR outstanding is between affiliated financial institutions. This is about twice as high as the

percent of tri-party outstanding that is between affiliates.<sup>71</sup> NCCBR also tends to be longer term and frequently uses non-U.S. Treasury collateral. Further, unlike the noncleared tri-party market segment where haircuts are generally applied to collateral, nearly 66 percent of NCCBR have a zero or negative haircut on the securities underlying the transaction. While this may reflect the prevalence of affiliate trading or margining done at the portfolio level, it also raises questions regarding counterparty credit risk management for NCCBR exposures.<sup>72</sup> As the prevalence of zero or negative haircut NCCBR exposures could potentially exacerbate counterparty credit risk and amplify losses in the event of a shock, this market segment warrants continued monitoring.

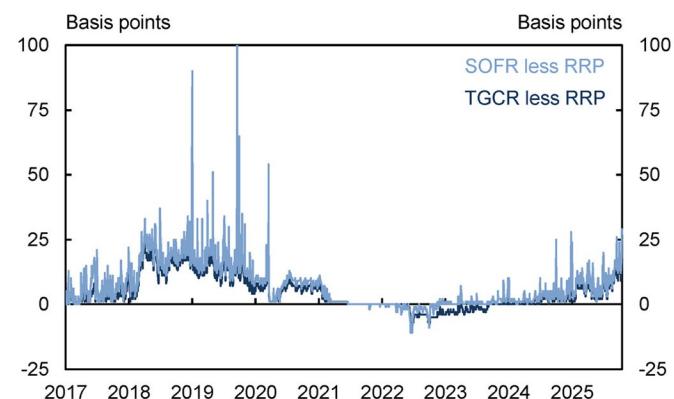
#### 4.1.1.3 Repo Transaction Volumes



Notes: Data as of October 15, 2025. Transactions with the Federal Reserve have been excluded from tri-party volume.

Source: OFR obtained through the OFR Short-term Funding Monitor.

#### 4.1.1.4 Overnight Repo Spreads



Note: Data as of October 15, 2025.

Source: FRBNY obtained through Haver Analytics, Inc.

## Money Market Funds

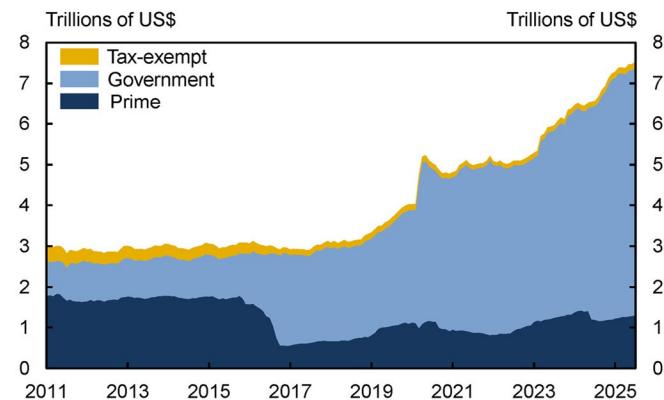
MMFs are major cash lenders in short-term funding markets. These funds serve as intermediaries between investors seeking daily liquidity with limited principal volatility and entities with short-term funding needs. There are three main types of MMFs: government, prime, and tax-exempt funds. Government MMFs invest almost exclusively in government securities and repos backed by government securities. Prime MMFs are permitted to invest in high quality credit-sensitive products, such as commercial paper, negotiable certificates of deposit (NCDs), and other short-term private debt securities, while also investing in government securities and repo. Tax-exempt MMFs primarily invest in short-term municipal obligations that are often exempt from federal income tax, and sometimes, state income taxes. MMFs can be further categorized as either retail or institutional depending on the client bases served.

MMFs perform liquidity and maturity transformation by offering shares that can be redeemed on a daily basis to investors while investing in short-term funding instruments that may be less liquid, especially during periods of market stress. This liquidity mismatch can incentivize investors to redeem preemptively during periods of market stress. In both 2008 and 2020, prime institutional MMFs experienced heavy redemptions that contributed to dislocations in short-term funding markets, and, in 2020, strains among tax-exempt MMFs contributed to stress in tax-exempt funding markets. These events led to extraordinary policy responses in 2008 when the Federal Reserve established liquidity facilities and the Treasury provided a temporary guarantee of MMFs, and in 2020, when the Federal Reserve again established facilities to stabilize short-term funding markets.

MMFs have undergone several rounds of reform since the GFC, and most recently, in 2024, MMFs implemented changes to comply with the SEC's 2023 amendments to MMF rules that were intended to improve MMFs' resilience during times of market stress.<sup>73</sup> Following implementation of these changes, assets at prime institutional MMFs, which have historically been the most run-prone segment, have declined while assets of prime retail and government MMFs continued to receive inflows, resulting in the sector's continued growth overall.

Indeed, as of July 2025, U.S. MMF net assets totaled \$7.5 trillion, up 15 percent from a year earlier (see **Figure 4.1.1.5**).<sup>74</sup> MMF assets growth remained strong amid market volatility and attractive yields offered by MMFs relative to bank deposit rates. Indeed, most asset inflows were concentrated in government MMFs, which have grown to \$6.1 trillion in July 2025 from \$5.2 trillion in July 2024 or approximately 16 percent. Net assets in prime retail MMFs stood at \$961 billion in July 2025, up 21 percent from last year, while net assets of prime institutional MMFs declined to \$342 billion in July 2025 from \$397 billion a year ago, down 14 percent. Net assets of tax-exempt retail MMFs stood at \$127 billion in July 2025 and tax-exempt institutional MMFs reached \$14 billion. While both types of tax-exempt funds have grown slightly, their total net assets remained modest relative to total MMF net assets.

### 4.1.1.5 MMF Total Net Assets by Type



Note: Data as of July 2025.

Source: SEC.

In July 2025, Treasury securities and Treasury repos were the largest MMF investment categories at \$2.7 trillion and \$1.9 trillion, respectively. This allocation reflects a shift in recent years away from ON RRP towards increased holdings of Treasury securities and repos that have more favorable returns. Since last year, MMFs have significantly increased their investments in centrally cleared repos, which have grown to approximately \$1.1 trillion in July 2025 from \$637 billion in July 2024. Still, about \$1.9 trillion of MMF repos are not centrally cleared. See **Sections 3.1 and 4.2.3** for a further discussion of central clearing of Treasuries.

Another key development is that interest in MMF exchange-traded funds (ETFs) and tokenized MMFs increased markedly in 2025. After launching in 2024, assets under management (AUM) for MMF ETFs stands at over \$4 billion.<sup>75</sup> As discussed further in **Section 4.2.2**, this reflects a broader trend of growing investor interest in ETFs. First introduced in 2021, tokenized MMFs managed net assets of approximately \$1.7 billion as of October 2025.<sup>76</sup> A tokenized MMF is a unique digital representation on a blockchain that represents shares in an MMF. Tokenizing MMF shares and utilizing cryptographically protected digital wallets to manage these tokens could potentially allow for greater MMF utility and new use cases, such as instantaneous changes in ownership. Stablecoins also hold their reserves in, among other things, short-term instruments and have grown in AUM during 2025. These are discussed further in **Section 4.1.6**.

### Short-Term Investment Vehicles

In addition to MMFs, other short-term investment vehicles (STIVs) also provide liquidity to short-term funding markets such as the U.S. commercial paper market, where STIVs hold more than 40 percent of the market.<sup>77</sup> Like MMFs, STIVs have structural characteristics that may amplify investor incentives to preemptively redeem shares in times of market uncertainty. Indeed, many STIVs have ownership interests that can be redeemed faster than the assets they hold can be liquidated. Further, most STIVs are permitted to invest in credit sensitive assets while operating with a stable net asset value (NAV) structure. The combination of these characteristics can incentivize investors to rapidly redeem assets during periods of market strain. Indeed, some STIVs have faced large-scale investor withdrawals during past episodes of stress. Asset liquidation in important funding markets, such as commercial paper, could contribute to financial instability. However, there is significant heterogeneity among STIVs, which may reduce some vulnerabilities and the likelihood of contagion. Finally, there are data gaps and limitations related to some types of STIVs that challenge the Council's monitoring of STIVs and the risks they pose to U.S. financial stability.

These STIVs include local government investment pools (LGIPs), dollar-denominated MMFs domiciled outside of the U.S. (offshore MMFs),

private liquidity funds, short-term investment funds (STIFs), and ultrashort bond funds. LGIPs are pooled investment products available to state and municipal governments. As of the second quarter of 2024, LGIPs had AUM of approximately \$900 billion.<sup>78</sup> Offshore MMFs are vehicles that invest in dollar-denominated short-term financial instruments and, as of year-end 2024, had AUM of approximately \$730 billion.<sup>79</sup> Private liquidity funds are structurally similar to MMFs but are only open to certain qualified investors and may be permitted to take greater risks. They often serve as the investment vehicle for large pools of cash collateral generated by securities lending activity and provide an additional source of income for large institutional lenders. Private liquidity fund AUM totaled approximately \$358 billion as of year-end 2024.<sup>80</sup>

STIFs are investment vehicles sponsored by banks or trusts that pool assets for eligible clients with whom the bank has a fiduciary relationship. STIFs sponsored by banks regulated by either the OCC or Federal Reserve had approximately \$350 billion in AUM as of year-end 2024.<sup>81</sup> Ultrashort bond funds are SEC-regulated mutual funds and ETFs that invest primarily in debt instruments with maturities of less than one year. Ultrashort bond fund AUM totaled approximately \$390 billion as of year-end 2024.<sup>82</sup>

### 4.1.2 Commercial Real Estate

CRE mortgage debt totaled \$6.2 trillion as of the second quarter of 2025. Approximately half of the debt is held by banks with the other half held by nonbank lenders, government-sponsored enterprises (GSEs), and other market participants. There are also interconnections across different holders of CRE mortgage debt. For example, banks lend to real estate investment trusts and funds that invest in CRE. Banks, insurance companies, asset managers, hedge funds, private equity (PE) companies and other specialized investors also invest in commercial mortgage-backed securities (CMBS) issued by agencies and private entities.

Following a period of post-pandemic deterioration, the CRE sector largely stabilized in 2025 as borrowing costs, vacancy rates, and asset values showed signs of steadyng in several property types. Indeed, the modest size of the most affected CRE sectors and broad resilience of

leveraged institutions exposed to CRE are factors that appear to mitigate the potential for CRE to pose systemic risks.

Banks' CRE loan delinquency rates remained low and decreased slightly between the first and second quarters of 2025. Delinquency rates in some CMBS markets, such as retail and lodging, stabilized in 2025 while those in other segments, like office, increased.<sup>83</sup> Issues to monitor going forward include potential challenges to some borrowers' repayment capacity due to high building operating costs and elevated refinancing risk as some CRE loans maturing or reaching date reset periods could be difficult to refinance, particularly in the office sector.

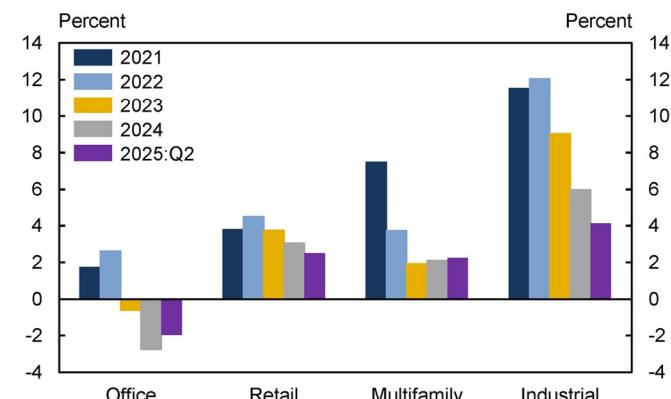
### CRE Fundamentals

Although CRE market conditions were somewhat mixed in the first half of 2025, some weaker segments of the market have shown signs of stabilization, including the office sector. The pace of vacancy rate increases is moderate as compared to 2021-24. Additionally, property values steadied although rent growth continued to slow across several property types.

Further, in recent years and across property types, net operating income (NOI), which a property generates after accounting for all operating expenses, was weighed down by rising vacancy rates, increasing operating costs, and tepid rent growth. In 2025, growth in NOI increased slightly in multifamily and was less negative in office than in 2024, which may suggest some stabilization in these sectors' cash flows (see **Figure 4.1.2.1**). That said, elevated operating costs may continue to weigh on borrowers' debt repayment capacity.

Although office remains the weakest property type, partly reflecting evolving demand for space as companies navigate use of remote work, 2025 showed some signs of decreased strain in office properties. The office vacancy rate rose slightly to 14.1 percent in the second quarter of 2025, but the pace of increase has eased in 2025 as compared to recent years (see **Figure 4.1.2.2**). Further, rent growth was positive at 0.8 percent in the year ending the second quarter of 2025, and prices were relatively stable after falling sharply from 2021 to 2024.

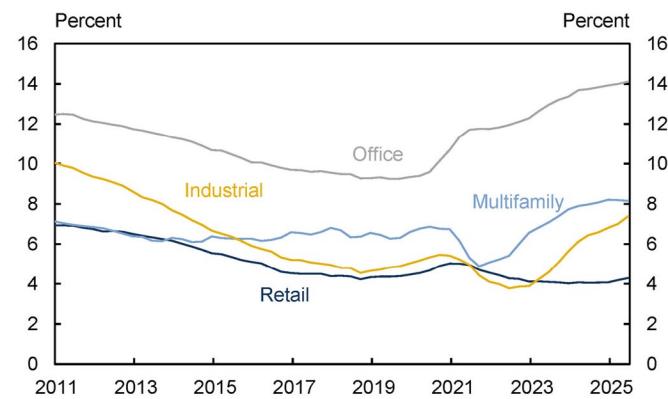
#### 4.1.2.1 Year-Over-Year Change in Net Operating Income by Property Type



Note: Data as of 2025:Q2.

Source: CoStar.

#### 4.1.2.2 Vacancy Rates by Property Type



Note: Data as of 2025:Q2.

Source: CoStar.

Another sign of improvement is the increase in leasing activity in larger markets. For example, the amount of newly leased space in New York City's Manhattan market reached nearly 16 million square feet in the first half of 2025, up nearly 15 percent from the first half of 2024 and slightly above 2019 levels.<sup>84</sup> A 15 percent increase in the volume of sales transactions nationwide through the first half of 2025 compared to the same period the prior year may also suggest some stabilization in office market conditions.

Multifamily vacancy rates eased in the first half of 2025, following three years of increase that reflected a surge in supply. The volume of units under construction has declined and demand has outpaced new construction in 2025, resulting in a slight

decline in the vacancy rate. Rent growth remains slow at 1 percent, which is slightly lower than the year before.

Further, newly added industrial space outpaced net absorption, pushing the vacancy rate higher. The industrial property vacancy rate reached 7.4 percent in the second quarter of 2025, above its 5 percent pre-pandemic rate but still in line with historical levels. The pace of new construction declined in 2024 and into 2025, which helped slow rising vacancies. Rent growth declined from very high levels.

Retail conditions remain stable. While demand has not been strong, supply growth also has been tepid. The vacancy rate of 4.3 percent in the second quarter of 2025 was up slightly from the year before but remained the lowest among the four major CRE property types.

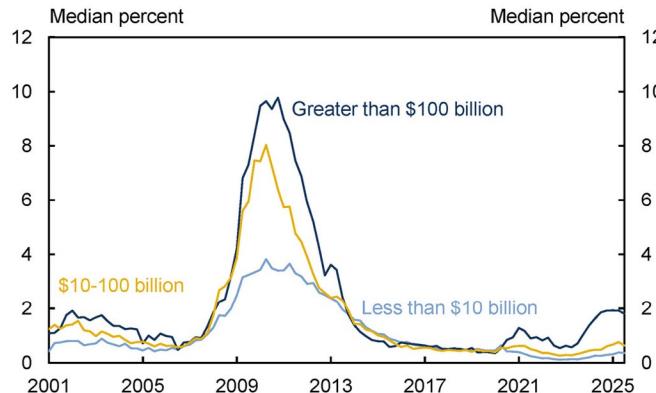
### CRE Credit Conditions

Overall bank loan delinquency rates remain modest and CRE loan exposure among banks stable. However, some pockets of credit pressure persist. In the \$1.8 trillion CMBS market, delinquencies in certain segments, such as retail and lodging, stabilized in 2025. However, the CMBS multifamily loan delinquency rate increased to 6.6 percent, up from 3.3 percent the year before, and the CMBS office loan delinquency rate remained historically high at 11.1 percent, up from 8.4 percent the year before. This weakness in the office sector drove the overall CMBS loan delinquency rate to 7.2 percent in September 2025, up from 6.7 percent the prior year.<sup>85</sup>

After increasing in recent years, the banking industry's CRE loan delinquency rate decreased slightly in the second quarter of 2025 and remains modest at 1.4 percent in the second quarter of 2025. CRE loan delinquency rates vary among small and large banks (see **Figure 4.1.2.3**).

The median CRE delinquency rate for the largest institutions—those with assets over \$100 billion—reached 1.8 percent in the second quarter of 2025. This level is well below that seen during prior periods of credit stress but above current levels for smaller institutions, which, in part, reflects more exposure to the office sector. Delinquency rates among smaller institutions remain much lower due to limited exposure to office properties in dense urban areas and generally more favorable CRE conditions in smaller markets.

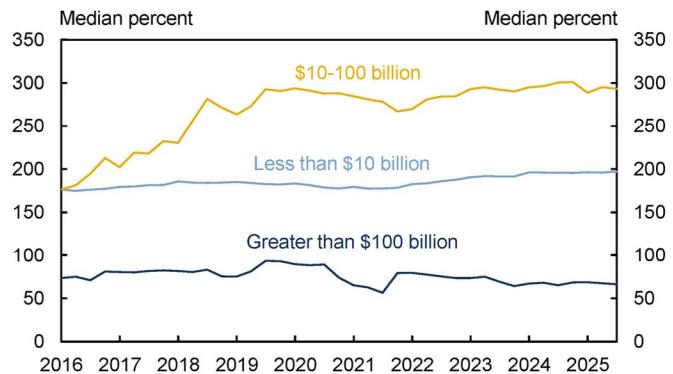
#### 4.1.2.3 Bank CRE Delinquency Rates by Asset Size



Note: Data as of 2025:Q2.

Source: FDIC.

#### 4.1.2.4 Bank CRE Concentrations by Asset Size



Notes: Data as of 2025:Q2. Concentrations are CRE loans as a percentage of tier 1 capital and the allowance.

Source: FDIC.

Although the volume of CRE loans held by the largest banks represents more than one-third of total CRE loans in the banking system, the exposure is modest relative to large banks' capital and allowance levels. In contrast, CRE concentrations remain elevated among mid-sized banks with assets between \$10 billion and \$100 billion (see **Figure 4.1.2.4**). However, as discussed in **Section 4.2.1**, banks have generally been effective in managing through the challenges associated with CRE concentrations. Overall, CRE loan exposure among banks was stable in 2025. The median CRE loan concentration of 198 percent of Tier 1 capital and allowances across all banks in the second quarter of 2025 was largely unchanged from one year ago.

Despite signs of sector stabilization, potential risks related to refinancing remain for the sector going

forward. Indeed, estimates suggest that \$936 billion of CRE debt is anticipated to mature in 2026, a nearly 19 percent jump from 2025, with a slightly higher amount, \$983 billion, due in 2027.<sup>86</sup> This maturity wall may present risks, particularly for weaker CRE segments like office, if borrowers are unable to secure additional financing, especially if tighter lending standards for CRE and a higher interest rate environment persist.

#### 4.1.3 Corporate Credit

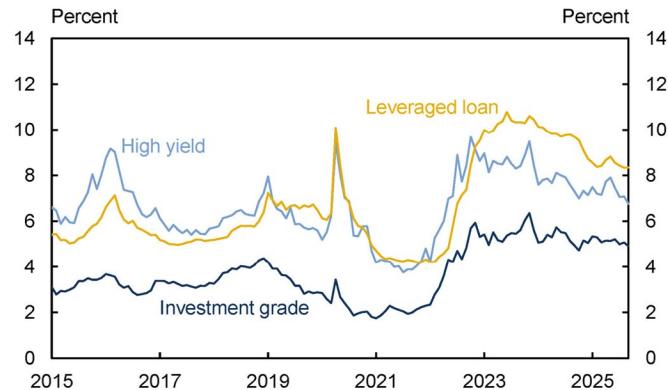
Well-functioning corporate credit markets play an important role in supporting business investment and helping to facilitate capital formation that fosters economic growth. Financial stability risks can arise, however, when unexpected financial or economic events negatively affect firms' abilities to service, refinance, or issue their debt, and corporate downgrades or defaults may transmit losses or stress to other corners of the financial sector. While strains from heightened market volatility were apparent in certain credit markets in April 2025, they were relatively short-lived, and credit market activity recovered as volatility subsided. Additionally, in aggregate, corporate fundamentals have also remained resilient; however, there are some signs of pressure on lower-rated borrowers.

Private credit has continued to grow and remains an important source of financing for both small and middle market companies. Private lenders also continue to increase commitments with larger companies that have traditionally utilized bank-arranged deals or broadly syndicated loan markets for capital financing.

#### Public Credit Markets

Aside from an uptick following the April market volatility, corporate bond and leveraged loan yields have remained relatively stable over the last year. Similarly, spreads over Treasuries saw a sizeable widening in early April but tightened to prior levels in May and generally continued to compress in the third quarter of 2025 (see **Figures 4.1.3.1** and **4.1.3.2**). U.S. corporates looking to access public markets in 2025 have faced both persistently high interest rates and evolving market sentiment related to international trade developments. Overall, U.S. corporations have been able to navigate this environment reasonably well with fundamentals remaining resilient in aggregate buoyed by positive earnings growth and limited debt growth.

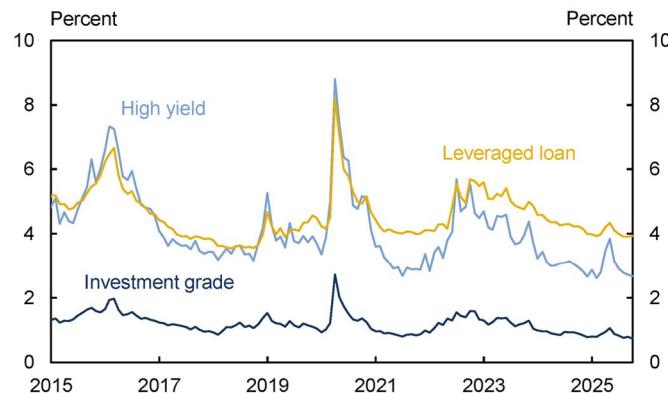
##### 4.1.3.1 Corporate Bond and Leveraged Loan Yields



Note: Data as of September 2025.

Sources: Bloomberg Finance L.P. and PitchBook Data, Inc.

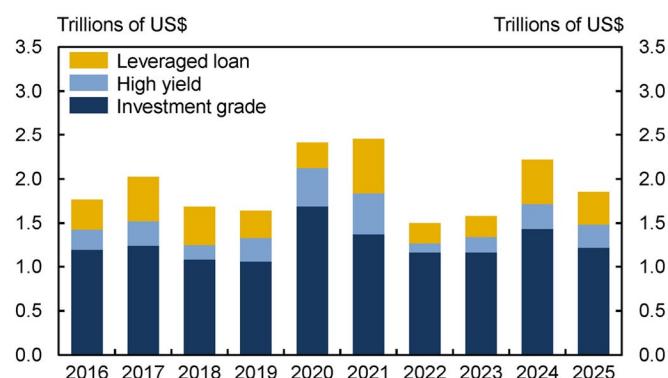
##### 4.1.3.2 Corporate Bond and Leveraged Loan Spreads



Note: Data as of September 2025.

Sources: Bloomberg Finance L.P. and PitchBook Data, Inc.

##### 4.1.3.3 Year-to-Date Gross Issuance



Notes: Data as of September 2025. Data as of December 31 for years 2016 through 2024.

Source: PitchBook Data, Inc.

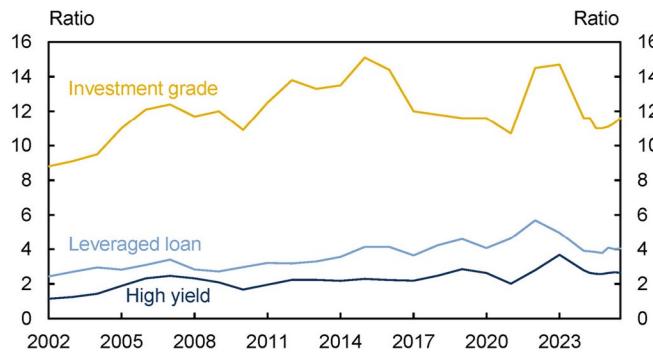
In 2025, corporate bond and leveraged loan issuance is on pace with recent years despite a notable decline in issuance for high-yield bonds and leveraged loans during the April volatility (see **Figure 4.1.3.3**). Indeed, when the volatility subsided, issuance rebounded across market segments.

Merger and acquisition and leveraged buyout activity remained tepid in 2025 as the PE industry continued to face challenges in exiting existing investments. As in 2024, the bulk of issuance activity in 2025 was from refinancings aimed at extending debt maturities.

Lower-rated firms with higher leverage and a greater share of floating-rate liabilities on their balance sheets, such as issuers in the leveraged loan market, experienced greater financial pressure in 2025. Higher borrowing costs have continued to put downward pressure on interest coverage ratios, especially for the lowest rated firms. In aggregate, however, interest coverage remains above historical lows across all categories of public borrowers (see **Figure 4.1.3.4**).

While default rates for high yield bonds remain subdued in 2025, those for leveraged loans are elevated compared to historical levels (see **Figure 4.1.3.5**). Distressed exchanges—where investors may be asked to take a small principal loss in exchange for receiving new debt, increased seniority, or higher yield—have been the dominant form of default so far in 2025 and have driven the elevated level of leveraged loan defaults.<sup>87</sup> While such exchanges allow firms to avoid bankruptcy proceedings in the short term, many of these businesses may default a second time and ultimately end up in bankruptcy. Downgrades of high-yield issuers ticked up in the second quarter of 2025 and outpaced upgrades throughout the second quarter as increasing numbers of speculative grade issuers faced pressure on gross margins. The level of bankruptcies among public firms has also edged up slightly in 2025 but remains broadly in line with prior years and well below peaks seen in the GFC (see **Figure 4.1.3.6**). Additionally, two recent bankruptcies of private auto-related firms have also attracted attention. While these events currently appear to be idiosyncratic, allegations of potential collateral fraud and opacity around the firms' funding arrangements with bank and non-bank lenders merit further attention.

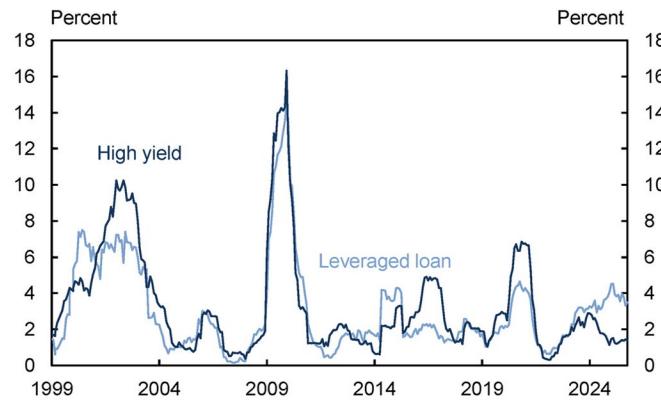
#### 4.1.3.4 Interest Coverage Ratios



Notes: Data as of 2025:Q2. Chart shows earnings before adjustments associated with interest, tax, depreciation, and amortization (EBITDA) over interest expense in the past 12 months. The investment grade series is market-value weighted and excludes outliers and financial firms. The leveraged loan series is a weighted average. The high yield series is a four-quarter moving average of the median of nonfinancial firms.

Sources: Barclays, Compustat, and PitchBook Data, Inc.

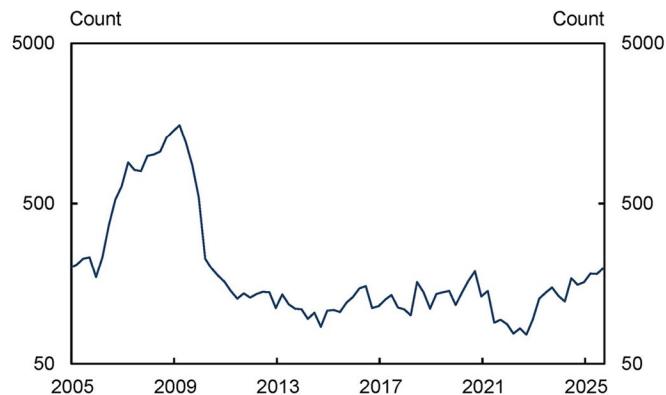
#### 4.1.3.5 Par-Weighted Default Rates



Notes: Data as of September 2025. Includes distressed exchanges.

Sources: J.P. Morgan and PitchBook Data, Inc.

#### 4.1.3.6 Bankruptcy Filings



Notes: Data as of 2025:Q3. Log scale applied on y-axis.

Source: S&P Global Market Intelligence LLC.

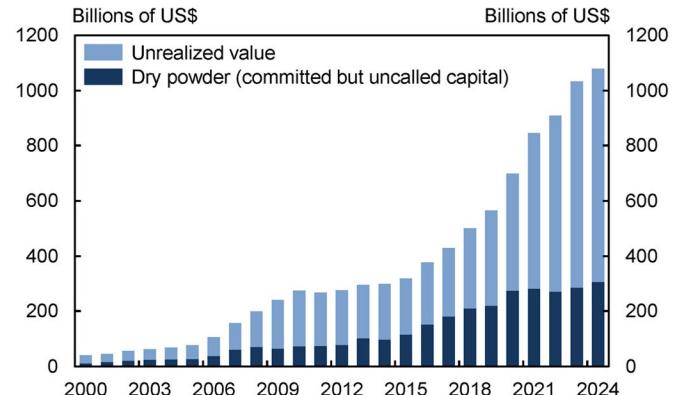
## Private Credit Markets

As noted above, private credit has established itself as an important source of financing for small and medium-sized firms, and non-bank private lenders have continued to increase commitments to larger businesses. In the United States, there is no uniform regulatory definition of “private credit,” but the term most frequently refers to credit investment vehicles that are funded by institutional investors and engage in direct lending to businesses. In addition to closed-end private credit funds, other non-bank investment vehicles that engage in private credit activity include business development companies (BDCs), interval funds, and securitized vehicles, such as private credit collateralized loan obligations (CLOs). Unlike most broadly syndicated loans, private credit loans are typically held to maturity with a focus on long-term performance. Notably, a lack of secondary market trading and limited available information on borrower fundamentals can make timely valuations challenging and result in limited transparency into the sector.

In North America, private credit funds have experienced substantial growth in recent years with estimated AUM of \$1.1 trillion as of year-end 2024, up from approximately \$565 billion at year-end 2019 (see **Figure 4.1.3.7**).<sup>88</sup> Indeed, private credit funds’ AUM is now of a comparable size to U.S. high-yield corporate bond and leveraged loan markets, which stand at \$1.2 trillion and \$1.4 trillion, respectively, as of year-end 2024.<sup>89</sup> Dry powder, which is the amount of money committed to private credit funds that has yet to be invested or “called” by fund managers, makes up \$305 billion of the \$1.1 trillion total. Further, BDCs have also experienced substantial growth, with estimated AUM growing from \$123 billion in 2019 to \$438 billion in 2024.<sup>90</sup>

Investor demand for private credit has been strong, driven in part by the market’s historically high returns. Indeed, private credit annualized returns during the past ten years have averaged approximately nine percent compared to nearly five percent for high-yield bonds and leveraged loans.<sup>91</sup> Investors typically receive higher yields to compensate for higher credit risk and lower liquidity. Indeed, one estimate indicates that default rates for private credit totaled 5.5 percent in the second quarter of 2025 as compared to 3.8 percent and 1.3 percent for leveraged loans and high-yield bonds, respectively.<sup>92</sup>

### 4.1.3.7 Private Credit Fund AUM



Notes: Data as of 2024. Data limited to North America.

Source: Preqin Ltd.

From the borrower’s perspective, private credit offers a relationship with one or a relatively small group of private credit lenders, more flexibility, greater ease and speed of execution, and fewer disclosure requirements relative to bank lending and the public markets. Furthermore, private credit provides features to borrowers such as Payment-in-Kind (PIK) that allows borrowers to defer interest payments and add them to the principal, which are not used as widely in bank loans and broadly syndicated loans. Interest in PIK provisions has grown in recent years as interest rates remained higher and some reports indicate that use of PIK increased as of the second quarter of 2025, nearing four-year highs.<sup>93</sup> A PIK provision can provide borrowers with significant flexibility during periods of high growth or can help borrowers weather temporary financial liquidity issues even though accrued interest increases borrower leverage. However, use of PIK provisions can mask credit problems, as delinquencies would not increase despite the borrower experiencing an inability to pay due to financial difficulties.

Unlike banks, which rely on on-demand deposits, private credit generally relies on longer-term, locked-up investor capital. As a result, any liquidity and maturity transformation risk would appear to be low. There has, however, also been a recent increase in semiliquid fund structures and investment vehicles that offer periodic (e.g., quarterly) redemption rights.

Private credit is increasingly interconnected with highly regulated financial institutions, including insurance companies and banks. For example,

banks are increasingly providing leverage to private credit funds often in the form of asset-based loans like warehouse funding lines or loan repo facilities, subscription credit lines that can be collateralized by investor commitments to the fund not yet called, and NAV loans collateralized by the fund's assets. While the exact amount of bank lending to private credit is unknown, new data suggest that banks' total loan commitments to private credit funds are approximately \$445 billion as of the second quarter of 2025.<sup>94</sup> Private credit funds along with other investors, such as credit hedge funds, also sell credit insurance to banks in the form of synthetic risk transfers against losses in a loan portfolio that allow banks to manage risk-weighted assets. While private credit presents a range of opportunities for investors and businesses, given its rapid growth, relative opacity, and increasing interconnections with the broader financial sector, continued monitoring is warranted.

### **Increasing Access to Private Assets**

In the last few decades, institutional investors have steadily increased their investments in private assets, seeking higher returns and greater diversification. This long-term shift was due to several factors. First, private markets provide an opportunity for sophisticated investors to identify attractive investment opportunities. Private markets also tend to be less liquid than public markets, which can lead to a premium for bearing illiquidity risk that endowments, pension funds, and insurance companies, with their long investment horizons, are ideally positioned to collect. Finally, the growth of private markets eventually made it difficult to hold fully diversified portfolios without participating in these markets.

There also has been more interest from retail investors to participate in private markets. Historically, restrictions on who can invest, high investment minimums, and high search costs have generally limited direct investment in private assets to institutional investors and high net worth individuals. More and more, asset managers are introducing new products for retail investors aimed at increasing access to private assets. This "retailization" of private markets may involve incorporating private assets in entities that are already available to retail investors, such as SEC-registered closed-end funds, BDCs, and ETFs.<sup>95</sup>

### **4.1.4 Household Credit**

The household sector is a central driver of demand for goods and services in the U.S. economy. In 2025, finances in the aggregate household sector have remained resilient, supported by a relatively healthy labor market and increased wage growth. Many household balance sheets have also benefited from gains in equity markets and home prices in recent years. Real income growth continued to bolster household finances with mean weekly real earnings increasing 1.1 percent year-over-year as of August 2025.<sup>96</sup> These gains reflect ongoing nominal wage growth and moderating inflation, which have helped sustain households' purchasing power despite continued elevation of household expenses.

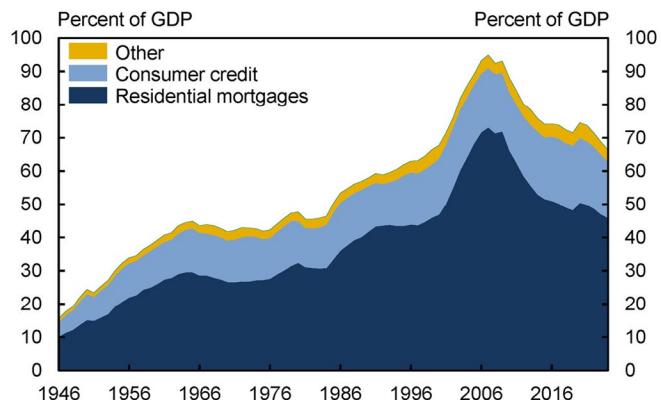
A key aspect of household balance sheets is consumer debt, which represents both a critical source of financing for families and a channel through which developments in the real economy and financial system interact. At over \$18 trillion, consumer debt is sizeable and widely held across financial intermediaries with depository institutions, the U.S. government, and nonbank lenders all maintaining significant exposures. Residential mortgages account for the largest share of household debt balances at \$12.9 trillion followed by auto loans (\$1.7 trillion), student loans (\$1.6 trillion), and credit cards (\$1.2 trillion). See **Section 4.1.5** for a more detailed discussion of mortgage markets.

While the size of the residential mortgage market far exceeds that of other consumer debt markets, trends in auto loan, student loan, and credit card debt provide a window into the overall state of household repayment capacity with potential impacts to the real economy. Households with elevated debt burdens may reduce consumption, dampening economic growth, or face rising repayment difficulties that can lead to losses for banks, nonbanks, and other investors.

### **Household Debt Levels and Debt Service Burdens**

Overall, household debt as a percentage of gross domestic product (GDP) continues to decline and sits at 68 percent, well below the peak of nearly 100 percent reached before the GFC (see **Figure 4.1.4.1**).<sup>97</sup> Over the last year, credit card balances rose 5.9 percent to \$1.2 trillion. They now stand at 4.0 percent of GDP, which is above COVID-19

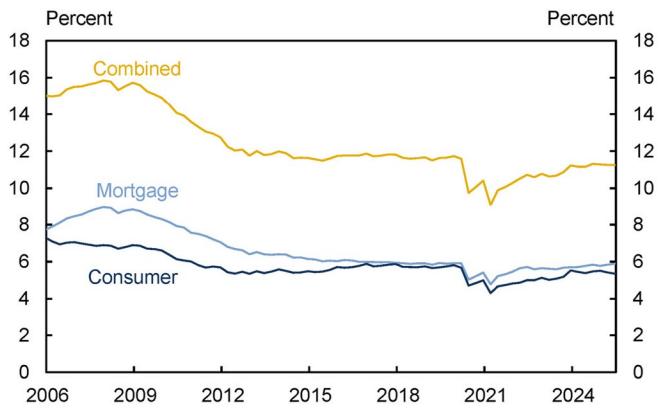
#### 4.1.4.1 Household Debt to GDP by Major Categories



Note: Data as of 2024.

Source: Federal Reserve Board obtained through FRED.

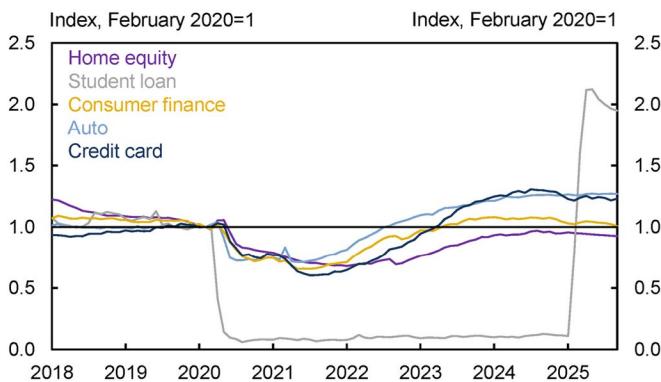
#### 4.1.4.2 Debt Service to Disposable Personal Income by Category



Note: Data as of 2025:Q2.

Source: Federal Reserve Board.

#### 4.1.4.3 Share of Balances 30+ Days Delinquent by Loan Type



Notes: Data as of September 2025. Values are seasonally adjusted and indexed to February 2020.

Source: Equifax Information Services LLC obtained through OFR.

pandemic levels but below peaks seen prior to the GFC. Over the same period, student loan balances have risen 3.3 percent to roughly \$1.6 trillion, or 5.2 percent of GDP, down from a pre-pandemic peak of 7.7 percent. Auto loan balances have remained flat over the past two years at approximately \$1.7 trillion, representing 5.6 percent of GDP, a share that has been broadly flat since the early 2000s.

Additionally, aggregate debt service burdens remain manageable as the household debt service ratio sits at 11.2 percent of disposable income, which is below pre-pandemic levels.<sup>98</sup> Meanwhile, the rise in debt service on consumer credit as a percentage of disposable personal income has leveled off after increasing from 4.3 percent in the first quarter of 2021 to 5.4 percent in recent years (see **Figure 4.1.4.2**).

#### Household Debt Delinquency Trends

Delinquencies remain elevated relative to pre-pandemic levels as the share of balances that are 30 or more days behind on payments is near or above pre-pandemic levels for all loan types (see **Figure 4.1.4.3**). However, growth in consumer debt delinquency rates has slowed and shown early signs of reversal in some categories. This can be attributed to consumer lenders tightening account management and underwriting standards that have occurred since the fourth quarter of 2022 to reduce risk exposure, coupled with moderation in inflationary pressure and improvements in real wage growth.<sup>99</sup>

In fact, noncurrent rates for credit cards and other consumer finance balances fell 10 to 20 basis points year-over-year while delinquency rates for auto loans and home equity loans were both virtually unchanged over the same period. These modest changes in delinquency rates over the past year are in contrast to the steep rise in delinquent debt shares from 2022 through 2024 when year-over-year growth in delinquency rates typically ranged from 50 to 100 basis points for credit cards and auto loans. Taken together, these trends suggest that the deterioration in consumer credit conditions from 2022 through 2024 has eased somewhat over the past year.

Meanwhile, consumer borrowing has shown recent signs of slowing. Aggregate consumer debt remained flat in real terms year-over-year

from September 2024 to September 2025 with real declines of over 1 percent in auto and consumer finance loans. Average credit card utilization rates have also fallen this year, particularly for subprime borrowers. These contractions in household borrowing may reflect, in part, more cautious consumer behavior.

Student loans are a notable exception to the recent stabilization in consumer debt delinquency. Federal forbearance policies amid the COVID-19 pandemic drove student loan delinquencies to historically low levels, but the federal payment pause ended in late 2023, and credit reporting for missed student loan payments resumed one year later.<sup>100</sup> Subsequently, the 30+ day delinquent share of student loan debt spiked to more than double its pre-pandemic rate this year, which is up from five years of near-zero delinquency rates (see **Figure 4.1.4.3**).<sup>101</sup>

Over 9 million student loan borrowers have transitioned to delinquency since credit reporting resumed. These delinquencies have driven steep declines in credit scores with the average VantageScore among affected borrowers dropping by nearly 100 points since the start of 2025 (see **Figure 4.1.4.4**). About a third of these borrowers have since returned to current status. However, adverse credit impacts can persist long-term, increasing borrowers' costs for other credit lines and limiting their access to new loans.

While the spike in student loan delinquencies raises concern due to potentially harmful impacts on borrowers, its implications for broader financial stability may be limited due to the modest amount of affected debt. Delinquent student loan borrowers hold \$387 billion in total consumer debt as of September 2025 with the largest amounts in student loans (\$186 billion) and mortgages (\$132 billion). These represent relatively small shares of the \$18 trillion in aggregate debt held by consumers; thus, elevated default rates on these debt balances are unlikely to pose systemic risks. However, student loan delinquencies should continue to be monitored for further deterioration and risks to household balance sheets.

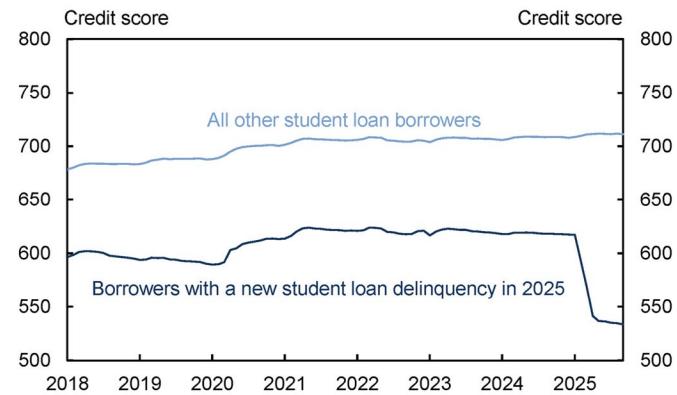
### **Enhanced Monitoring of the Household Sector**

Understanding how households' balance sheets may be affected by a potential economic shock

is a key aspect of monitoring financial stability. As noted, financially resilient households can withstand shocks, maintain essential consumption, and avoid costly debt cycles—all elements critical for long-term and sustainable economic expansion. To this end, the OFR has developed a novel methodology to enhance timely monitoring of financial stress in the household sector.<sup>102</sup> The OFR Household Liquidity Monitor provides high-frequency estimates of the household liquidity conditions by nowcasting infrequent data on household balance sheets.<sup>103</sup> It attempts to fill a critical data gap in household liquidity measurement. Currently, the OFR

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#### **4.1.4.4 Average Credit Score Among Student Loan Borrowers by New Delinquency Status**

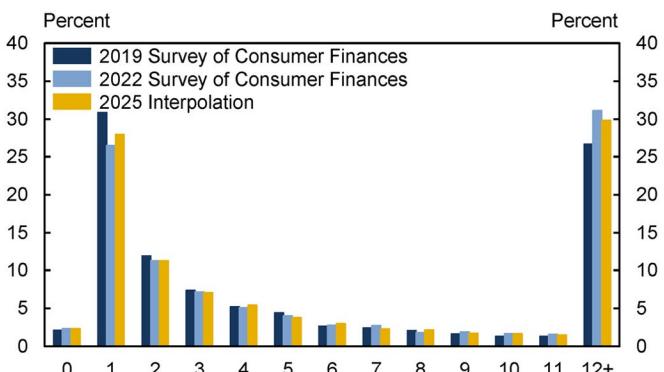


Note: Data as of September 2025.

Source: Equifax Information Services LLC obtained through OFR.

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#### **4.1.4.5 Projected Months of Covered Expenses for Households**



Note: Months of liquidity has been collapsed into 13 bins based on the number of months a household can, at most, use their savings to cover expenses.

Sources: Bureau of Labor Statistics, Federal Reserve Board, Federal Reserve Survey of Consumer Finances, OFR, and Wheat, C., Deadman, E., & Sullivan, D. M. (2025, July 17). *Household Finances Pulse through May 2025: Bank balances are flat but total savings are growing again*. JPMorganChase Institute. <https://www.jpmorganchase.com/institute/all-topics/financial-health-wealth-creation/household-finances-pulse-through-may-2025>.

Household Liquidity Monitor shows that estimated household liquidity conditions appear to have improved compared to 2019 (see **Figure 4.1.4.5**). These projections provide useful insight into the current state of household liquidity buffers.

## 4.1.5 Residential Real Estate

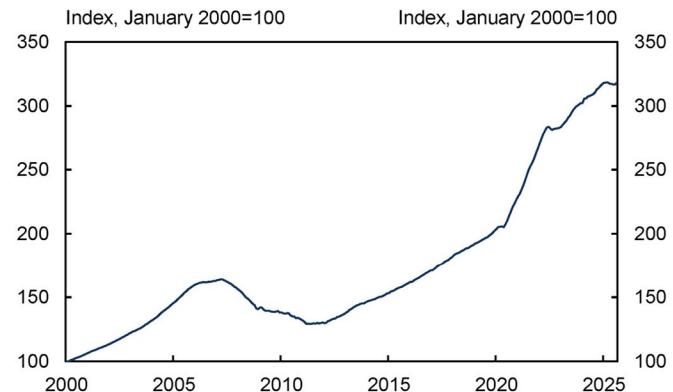
RRE is a large and important part of the U.S. economy, standing at nearly \$60 trillion in total assets as of the second quarter of 2025.<sup>104</sup> Significant price appreciation in recent years has resulted in high levels of equity for many homeowners but that price appreciation has also combined with high interest rates to make purchasing a home more difficult. The result has been a sluggish single-family real estate market. New home sales declined in the first half of 2025 relative to the first half of 2024, and existing home sales are currently hovering slightly above the lowest levels since the GFC. Housing starts and new permits both declined in the first half of 2025, suggesting that the near-term outlook will remain muted.

House prices have risen 55 percent nationally since the start of the COVID-19 pandemic in March 2020, according to the FHFA House Price Index® (HPI) (see **Figure 4.1.5.1**). The fastest growth occurred in 2020 and 2021 when mortgage interest rates fell sharply in response to pandemic-related factors. More recently, house prices have weakened. The FHFA HPI shows that the rate of change of house price growth has declined since that 2020-21 period, and the most recent release showed only 2.3 percent annual growth in the 12 months ending August 2025. This is the slowest year-over-year growth since April 2012. The seasonally adjusted August HPI rose by 0.4 percent versus the July 2025 value. Prior to the August growth, the period from April through July of 2025 was the weakest four-month period for the HPI since 2011.

Slowing house price growth has been evident across all geographic regions, but the Pacific, West South Central, Mountain, and South Atlantic regions have seen the most drastic slowing, and some areas have seen negative year-over-year changes in home prices.

Affordability challenges affect both potential new homeowners and existing homeowners. Much of the public dialogue has focused on potential new homeowners being shut out of the housing market

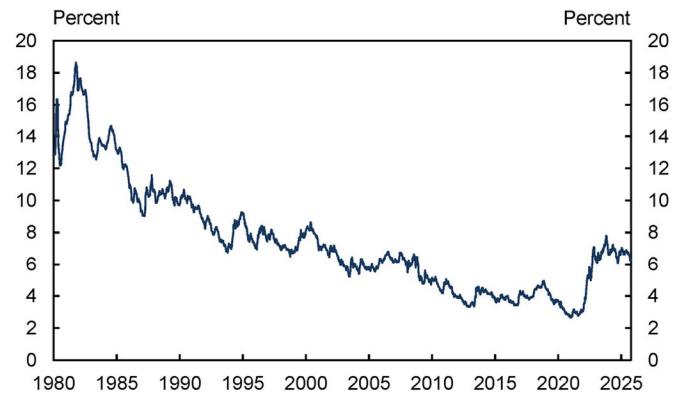
### 4.1.5.1 House Price Index



Note: Data as of August 2025.

Source: FHFA obtained through FRED.

### 4.1.5.2 30-Year Fixed Rate Mortgage Interest Rate



Note: Data as of October 9, 2025.

Source: Freddie Mac obtained through Bloomberg Finance L.P.

by high downpayments and high interest rates, but existing homeowners are also affected in negative ways by rising home prices despite an increase in their equity (see **Figure 4.1.5.2**). High mortgage rates may discourage moving and taking on a new mortgage, but property taxes and homeowners' insurance payments have also increased significantly in the last five years. Property taxes are based on assessed property values, and homeowners' insurance premiums are influenced by replacement costs and other factors.

The Intercontinental Exchange (ICE) reports that property tax payments increased by 5 percent in 2024 and 22 percent over the last five years while average homeowners' insurance payments increased by 14 percent in 2024 and 61 percent over the last five years.<sup>105</sup> This leads to higher all-in mortgage payments for borrowers even if they have a fixed-rate

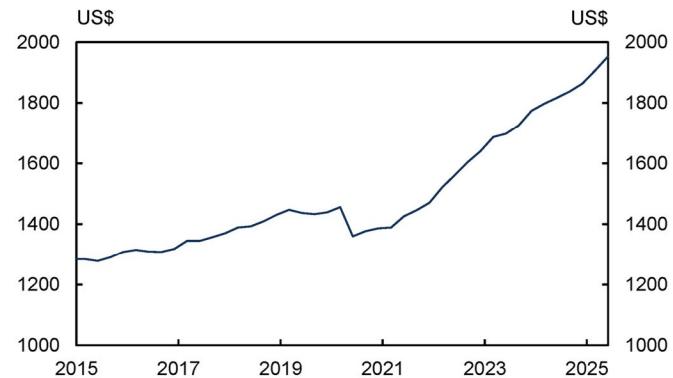
mortgage with a lower rate. The national average monthly payment on outstanding mortgages, which includes taxes and insurance for borrowers that use an escrow account, rose by 7 percent in the 12 months ending June 30, 2025, and by 34 percent nominally since the start of the COVID-19 pandemic in March 2020 (see **Figure 4.1.5.3**). While these market conditions present regional affordability and liquidity challenges, elevated equity levels have buoyed many homeowners.

Borrowers in some areas prone to natural disasters continue to face significant increases in the price of insurance and decreased availability of insurance in the primary market. However, there have been some notable changes in state regulatory policies that have improved the outlook for insurance availability, particularly in Florida and California. Florida enacted a series of legislative changes in 2022 and 2023 to address litigation costs, market instability, and other factors that were increasing availability challenges. Florida officials have reported that 15 new insurers have entered the market since these regulatory reforms were passed. The quick entry of these insurers to the Florida market following these regulatory changes highlights the importance of ensuring fair and effective regulation without placing too heavy of a regulatory burden on markets. California has also made changes to improve its insurance market mainly by allowing its insurers to use predictive catastrophe modeling to better assess risks. Previously, California had been one of a few states to prohibit the use of such modeling despite the frequency of natural disasters in the state. This should enable insurers to more accurately price their actual risk exposure, which should make the California market more appealing to insurers.

### **Primary Mortgage Market**

Total mortgage originations showed positive year-over-year growth as of the second quarter of 2025, spurred by falling interest rates and higher refinance volume (see **Figure 4.1.5.4**). Refinance originations in the first half of 2025 were 64 percent higher than the first half of 2024 mainly from a pickup in volume as mortgage interest rates fell. Purchase mortgage volume in the first half of 2025 rose modestly by 2 percent from the first half of 2024. Even with the boost to refinance volume from lower mortgage interest rates,

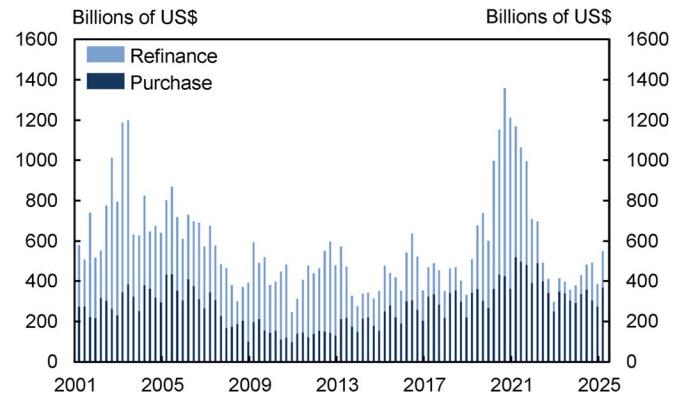
#### **4.1.5.3 Average Monthly Mortgage Payment**



Notes: Data as of 2025:Q2. Average monthly mortgage payment is calculated using outstanding mortgages.

Source: FHFA obtained through the National Mortgage Database.

#### **4.1.5.4 Quarterly Mortgage Originations**



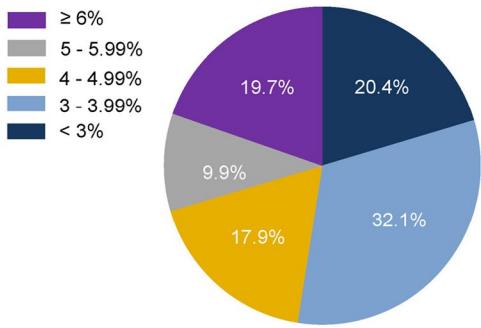
Note: Data as of 2025:Q2.

Source: Mortgage Bankers Association obtained through Haver Analytics, Inc.

refinance activity remains below its historical median, and mortgages for home purchases continue to represent the majority of originations. Approximately half of outstanding mortgages still have interest rates at or below 4 percent (see **Figure 4.1.5.5**). These borrowers are less likely to refinance or move, putting downward pressure on housing supply.

Mortgage delinquency rates bottomed out in 2021 and have been gradually rising since. However, delinquencies for conventional loans remain below historical averages and concerns are mitigated by the significant build-up of equity in recent years. The gap between performance of conventional loans and Federal Housing Administration (FHA) loans has expanded relative to January 2024 as the performance of FHA-insured loans have

#### 4.1.5.5 Outstanding Mortgages by Interest Rate



Note: Data as of 2025.Q2.

Source: FHFA obtained through the National Mortgage Database.

been deteriorating more rapidly. Higher levels of mortgage delinquencies can be financially stressful to mortgage servicers, particularly for Government National Mortgage Association (Ginnie Mae) MBS transactions given the more extensive advancing requirements of that program.<sup>106</sup> Higher delinquencies can also increase distressed sales and adversely impact home values as happened during the GFC. Closely monitoring and managing mortgage performance is critical to maintaining the health of the mortgage finance system.

#### Nonbank Mortgage Companies

Nonbank mortgage companies continued to gain market share from banks over the last year as the share of nonbank originations and servicing reached record highs. Nonbanks serviced 59 percent of outstanding mortgages as of the second quarter of 2025 compared with just 20 percent in 2013. Additionally, the concentration of nonbank mortgage servicers as a percentage of top servicers grew substantially over the same period as a result of the number of nonbank servicers in the top 20 doubling from just six in 2013 to 12 in 2025. Nonbank, residential mortgage originators also continued to gain market share with nonbanks originating approximately 64 percent of loans in the second quarter of 2025 as compared to 42 percent in 2014. Nonbank originator concentration has also increased with nonbanks comprising nine of the 10 largest originators as of the second quarter of 2025 as compared to just two nonbanks in the top 10 in 2013.

Nonbank mortgage companies bring both strengths and vulnerabilities to the mortgage market. Nonbank mortgage companies have

strengthened the market by serving as key mortgage originators and servicers for historically underserved borrowers, and some nonbank mortgage companies have developed expertise in certain products or operations. However, nonbank mortgage companies may be more vulnerable to certain market conditions than traditional banks, and the expanding role of these nonbank companies in the mortgage origination and servicing businesses may increase potential systemic risks to the U.S. financial system.

Indeed, as nonbank mortgage companies are often monoline businesses, their profitability can fluctuate with changes in mortgage demand, interest rates, and mortgage defaults. Moreover, in contrast to the bank lending and servicing model, nonbank mortgage companies lack access to deposits for short-term funding. Further, though their business models vary, many nonbank mortgage originators often rely on secured short-term wholesale funding that are typically uncommitted lines that can be quickly restricted or reduced in times of stress. This can lead to liquidity risk, which can be exacerbated by the leverage that some nonbank mortgage companies carry and their obligations to make servicing advances. Nonbanks also do not have access to liquidity backstops that could provide bridge funding if traditional lines of credit are tightened or not renewed, and nonbank mortgage companies' primary assets, which are mortgage loans held for sale and mortgage servicing rights (MSRs), may also prove illiquid in times of severe stress. Further, servicers often must advance interest and principal as well as loan-level payments for taxes and insurance and, therefore, can face liquidity pressure during periods of low origination volumes and high delinquencies.

Given these potential vulnerabilities and that nonbank mortgage servicers carry out critical servicing functions for the mortgage market, they could also represent a transmission mechanism by which a shock could be amplified through the financial system. Indeed, stress in the nonbank mortgage sector could lead to disorderly servicing transfers. A stressed nonbank mortgage servicer may fail to apply collections properly, make required advances, mitigate losses, or perform other servicing activities. Borrowers may subsequently suffer from disruptions in the servicing of their mortgages, and credit

guarantors and insurers may experience sizeable losses. In the event of failure, transferring one or more large nonbank mortgage company's servicing portfolios to another servicer could be difficult to accomplish in a timely and effective manner during periods of stress as the transfer process can be lengthy and complicated.

### **Secondary Mortgage Market**

The secondary mortgage market serves many functions within the housing finance system. In addition to the buying and selling of standardized mortgage securities, prevailing secondary market prices directly influence mortgage rates for new borrowers. The agency MBS market remains strong with agency MBS issuance up 14 percent year-over-year in the first half of 2025. Agency MBS valuations were pressured briefly in the spring as spreads over Treasuries widened in the beginning of April. Even so, MBS spreads over Treasuries have narrowed since then and are roughly unchanged since the end of 2024.

The Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) (together, the GSEs) went through significant changes in the first half of 2025 but continued to build capital. FHFA instituted material management and Board changes at the GSEs with a heightened focus on improving profitability and eliminating fraud. Together, the GSEs guaranteed more than \$6.4 trillion of outstanding single-family mortgages as of July 31, 2025, which is more than 57 percent of all single-family residential mortgage debt outstanding. Both GSEs continue to report a regulatory capital deficit, but the companies generated more than \$18.8 billion of combined net income in the first nine months of 2025, growing their combined net worth amounts to \$173.1 billion.

#### **4.1.6 Digital Assets**

EO 14178 notes that the digital asset sector plays an important role in innovation and economic development in the United States, as well as the nation's global leadership. The sector enables global, secure, and efficient financial transactions via distributed ledger technology (DLT) used in digital assets and decentralized finance platforms. A primary policy objective of the Administration and several member agencies of the Council is to facilitate the responsible growth and use

of digital assets, blockchain technology, and related innovations across all sectors of the economy. Consistent with the July 2025 report by the President's Working Group on Digital Asset Markets (Digital Asset Report), this report defines a digital asset as any digital representation of value recorded on a distributed ledger.<sup>107</sup>

Since the public announcement of bitcoin in 2009, the digital asset ecosystem has undergone substantial growth, expanding from a niche area of interest into a significant market facilitating large volumes of transactions. Although retail participants were the primary drivers of early adoption, institutional firms have increasingly pursued exposure to the sector. This institutional involvement includes direct financial investment in digital assets and their underlying protocols, venture investment in companies within the ecosystem, and the internal development of products enabled by blockchain and other DLTs. Additionally, in early 2024, the SEC's approval of spot digital asset exchange-traded products introduced a new vehicle for investors to gain such exposure without a wallet or direct custody of the assets, further reflecting the expanding growth of the market to retail investors.

Digital asset markets are notable for their global, cross-jurisdictional nature, which facilitates transactions on a worldwide basis. While this global accessibility presents certain efficiencies, it also creates challenges for measuring the scale of activity within any single jurisdiction. Despite these measurement challenges, data from public blockchains indicate that in early 2025, the number of successful monthly transactions reached 3.8 billion, representing a 96 percent year-over-year increase.<sup>108</sup>

### **Regulatory Framework and Market Structure**

U.S. regulatory agencies have sought to use existing legal frameworks to classify digital assets. The CFTC, for instance, recognized that certain digital assets like bitcoin and ether are commodities. Meanwhile, the SEC has treated other digital assets as securities based on their structures, methods of distribution, and uses. In the absence of a comprehensive classification system, market participants must navigate these varied regulatory interpretations and guidance. Establishing a clear taxonomy is important for

the responsible development of the digital asset ecosystem and for ensuring sufficient consumer and investor protection. A similar need for clarity exists regarding the classification of digital assets for federal income tax purposes.<sup>109</sup>

The Digital Asset Report sets forth a comprehensive set of recommendations to enhance regulatory clarity and adopt a pro-innovation approach towards digital assets and blockchain technologies. The recommendations include that the SEC and CFTC use their existing authorities to enable the trading of digital assets at the federal level by providing clarity to market participants on issues such as registration, custody, trading, and recordkeeping as well as to allow innovative financial products to reach consumers through the use of tools such as safe harbors and regulatory sandboxes. Accordingly, the SEC has launched its Project Crypto Initiative, and the CFTC its Crypto Sprint Initiative, to implement these recommendations.

Congress is considering market structure legislation for digital assets that could establish jurisdictional boundaries between the SEC and the CFTC for the oversight of digital asset markets. Furthermore, it could direct the SEC and the CFTC to jointly promulgate rules to permit portfolio margining across digital asset classes. It could also include provisions protecting the right to self-custody of digital assets. Lastly, it could increase capital efficiency for investors participating in these markets and establish legal clarity for the accounting and balance sheet treatment of digital assets held by banking institutions. Continued monitoring of regulatory developments and the subsequent actions of market participants will be important to understand how benefits and risks evolve.

## Tokenization

An increasing number of issuers are tokenizing assets by using blockchain or other DLT to represent and record the ownership of assets such as securities, creating tokenized securities. This approach is intended to increase efficiency in the transfer of ownership, enhance liquidity, and broaden investor access. The ability to tokenize assets can enhance fractional ownership and trading in previously illiquid assets, as well as improve collateral and risk management. Importantly, tokenized securities

are subject to applicable securities laws, and any offer or sale must either be registered with the appropriate regulators or qualify for a legal exemption.<sup>110</sup> With the increasing adoption of tokenization, the focus will continue to be on the benefits, risks, and regulatory implications.

## Stablecoins and Payments

Stablecoins are digital assets designed to maintain a stable value relative to a reference asset, such as a fiat currency. Stablecoins pegged to the U.S. dollar are intended to function as a means of payment and store of value, leveraging the features of digital assets while referencing the stability of the national currency. On July 18, 2025, the GENIUS Act was enacted to establish a federal prudential framework for certain payment stablecoin issuers.<sup>111</sup> The legislation is designed to provide regulatory clarity for these arrangements and incentives to onshore stablecoin innovation to the United States.

The GENIUS Act establishes a licensing regime and regulatory framework for payment stablecoin issuers, and the legislation explicitly subjects such licensed issuers to the Bank Secrecy Act (BSA) and anti-money laundering (AML) laws and regulations. To promote financial stability and transparency, the framework requires that issuers maintain reserves composed of highly liquid assets, such as U.S. Treasuries, that are sufficient to fully back their outstanding stablecoins. Issuers are also mandated to publish monthly reports on the composition of these reserve assets.

Further, the framework protects consumers by prioritizing the claims of payment stablecoin holders in an insolvency proceeding, prohibiting the rehypothecation of reserves except for limited purposes, and requiring that third-party custodians segregate reserve assets from their own funds. Additionally, the GENIUS Act provides statutory clarification that payment stablecoins issued by permitted payment stablecoin issuers (as defined in the GENIUS Act) are treated as neither securities nor commodities. This classification is intended to facilitate the adoption and use of stablecoins for payments by consumers and businesses in the United States and globally.

The continued use of U.S. dollar-denominated stablecoins is expected to support the role of the U.S. dollar in the international financial system

over the next decade. Thus, the GENIUS Act's framework represents a critical first step toward establishing a comprehensive regulatory structure for the digital asset industry.

## **Banking Sector**

Banking institutions are engaging with the digital asset industry through two main channels: first, by providing core banking products and services to digital asset market participants, and second, by facilitating customer access to digital asset markets through various functions like safekeeping and custody services that include trade execution and transaction settlement. A clear regulatory framework is required to ensure that these institutions can continue to engage in responsible innovation. This includes facilitating customer engagement with digital assets and utilizing DLT in a manner consistent with safe and sound banking practices and in compliance with applicable laws and regulations.

The U.S. risk-based capital framework does not contain explicit provisions for the treatment of digital asset exposures. Consequently, under the current capital rules, the risk weight assigned to a digital asset exposure would be determined by several factors and depend on the nature of the particular exposure.

Further, certain digital asset firms may seek to obtain a bank charter. Such a charter would enable these firms to expand their service offerings within a prudentially regulated environment. Furthermore, obtaining a bank charter may confer legal eligibility to request access to a Federal Reserve Bank master account and associated payment services, which may reduce operational costs, processing delays, and counterparty risks.

## **Illicit Finance**

While stablecoins and other forms of digital assets present a promising use case for enhancing the efficiency of cross-border payments and financial transactions, they may also be abused to facilitate illicit financial transactions. Similar to other mediums of exchange, certain features of digital assets include the ability to conduct rapid cross-border transfers and a perceived degree of anonymity, and these features can be exploited by illicit actors to facilitate money laundering and terrorist financing, as well as

other predicate offenses, crimes, and fraud. The federal government's approach to mitigating these illicit finance risks in the digital asset ecosystem is based on understanding threat actors' misuse of the assets and the features of the underlying technology. Certain industry estimates indicate that the vast majority of on-chain digital asset transaction volume is associated with legitimate activities; illicit activity represents a smaller share of the overall digital asset market.<sup>112</sup> The scale of such activities and their implications for the financial system overall are important considerations for continued monitoring by regulators. The Digital Asset Report recommends that U.S. law enforcement agencies should have the tools and authorities to hold those using digital assets for illegal activities accountable and that these tools should never be misused to target the lawful activities of law-abiding citizens.

## **Continued Monitoring and Further Action**

The Council can serve as a valuable forum for interagency information sharing and monitoring with a focus on understanding interconnections between digital assets, financial institutions, markets, and households. Council member agencies will work to faithfully and expeditiously implement the provisions of the GENIUS Act as required by law. The Digital Asset Report contains recommendations for Congress and various government agencies, including certain Council member agencies, to enable innovation and American leadership in digital financial technology.

## **4.2 Financial Institutions**

### **4.2.1 Depository Institutions**

The U.S. banking system is composed of a diverse set of institutions including community banks, regional banks, G-SIBs, and other large banks. Depository institutions, which also include credit unions, deliver critical services to the U.S. economy and play an indispensable role in the global financial system.

## **Banking Sector**

The resilience of the banking system is essential to the provision of credit to retail and commercial borrowers; holding of customer deposits; the ability of firms to raise capital or hedge risk; and

the availability of asset management, custody, and payments services. Over the past year, this resilience has been supported by healthy growth in revenues and robust profitability (see **Figure 4.2.1.1**). Liquidity buffers remain adequate and regulatory capital ratios remain close to long-term peaks (see **Figure 4.2.1.2**).

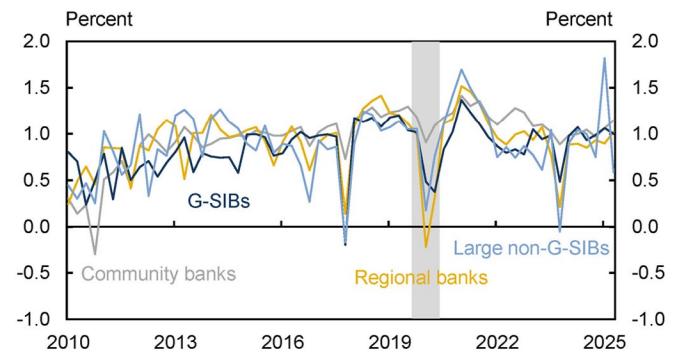
Bank loan growth, which has been modest in recent years, picked up in the first half of 2025. In the first six months of 2025, loan growth at large banks improved for most segments of their aggregate portfolios. Loan growth strengthened even though respondents to the July 2025 Senior Loan Officer Opinion Survey (SLOOS) reported that, on balance, standards are currently at the tighter end of the range for all loan categories. Banks also reported weaker demand across loan categories included in the survey. The survey also finds that large banks were slightly more likely than other banks to relax lending standards including for CRE loans.<sup>113</sup>

Delinquency rates on average are below rates that prevailed in the period prior to the COVID-19 pandemic. Where nonperforming loan (NPL) rates are slightly elevated, notably in CRE and consumer credit, banks with concentrations in these segments remain exposed to further weakening of credit quality. However, even in these segments, NPL and net charge-off rates have stabilized and have stayed well below the rates seen in prior periods of credit stress (see **Figure 4.2.1.3**).

Despite uncertainty about the outlook for interest rates during the first half of 2025, net interest income benefited from a decline in funding costs and the recovery in loan growth (see **Figure 4.2.1.4**). Unrealized losses on banks' securities portfolios decreased but remain sensitive to the level of interest rates. G-SIBs and other large banks also saw robust growth in noninterest income, supporting their profitability.

Community banks, which provide essential financial services to many American families and businesses, tend to rely more on net interest income than their larger peers. Although higher noninterest expense points to a rising cost of doing business for community banks, loan growth, favorable funding costs, and loan yield trends supported an increase in profitability. Additionally, regulators are considering measures

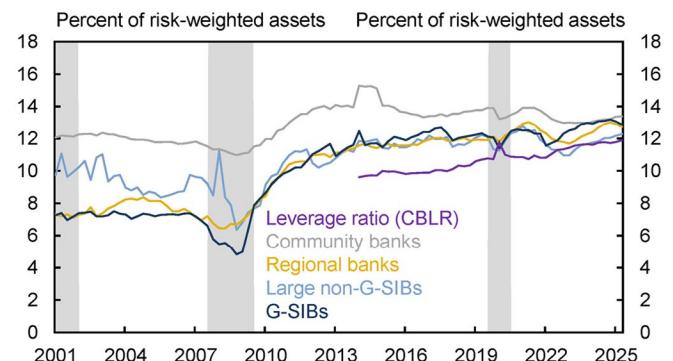
#### 4.2.1.1 Return on Assets



Notes: Data as of 2025:Q2. Return on assets is equal to net income divided by average assets. Community banks have less than \$10 billion in assets, regionals have total assets between \$10B and \$250B, G-SIBs and large non-G-SIBs have total assets above \$250B. Gray bar signifies National Bureau of Economic Research (NBER) recession.

Sources: FR Y-9C, Call Reports, and NBER.

#### 4.2.1.2 Common Equity Tier 1 Ratios



Notes: Data as of 2025:Q2. Since 2014:Q1, the numerator is CET1 capital (2015:Q1 for non-advance approach BHCs). Prior, the numerator was Tier 1 common capital. The denominator is risk-weighted assets. Leverage ratio is for CBLR filers and is calculated as Tier 1 capital divided by average consolidated assets. Gray bars signify NBER recessions.

Sources: FR Y-9C, Call Reports, and NBER.

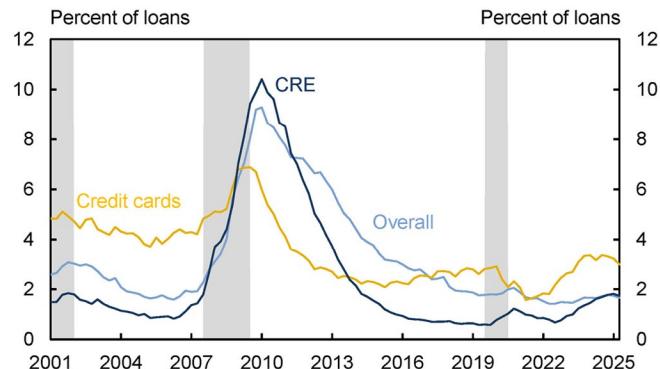
to support the strength and vitality of these banks and the communities they serve, as discussed in **Section 3.3**.

Bank mergers increased in 2025. Indeed, the value of deals announced in 2025 exceeded annual deal values for each of the previous three years. Further, the third quarter of 2025 saw more deals than any quarter since the third quarter of 2021.<sup>114</sup>

#### G-SIBs and Large Non-G-SIBs

U.S. G-SIBs and other large banks with more than \$250 billion in assets are important intermediaries in global finance, including through the provision of payments services to domestic and foreign

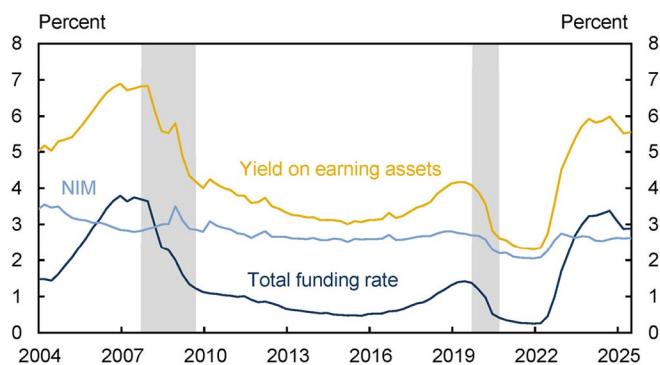
#### 4.2.1.3 Delinquency Rates on Selected Loans



Notes: Data as of 2025:Q2. Banks with total assets greater than or equal to \$10 billion. Includes all loans in foreign and domestic offices. Auto loan series became available in 2011:Q1. Gray bars signify NBER recessions.

Sources: FR Y-9C, Call Reports, and NBER.

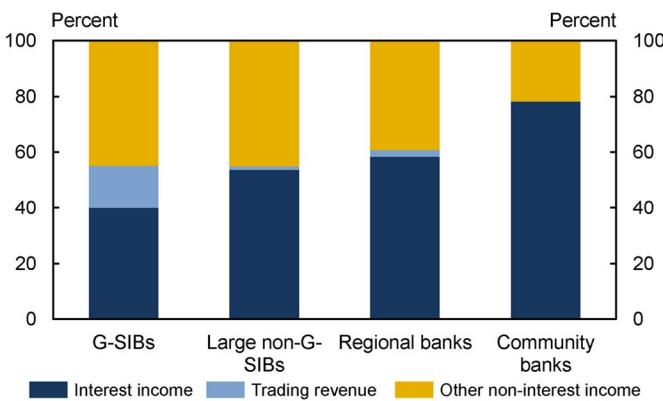
#### 4.2.1.4 Total Funding Rate, Yield on Earning Assets, and NIM



Notes: Data as of 2025:Q2. Total funding rate: total interest expense divided by liabilities. Yield on earning assets: total interest rate divided by interest earning assets. Gray bars signify NBER recessions.

Sources: FR Y-9C, Call Reports, and NBER.

#### 4.2.1.5 Income Composition (2024)



Note: Data as of 2024.

Sources: FR Y-9C and Call Reports.

customers and in Treasury and repo markets. They also deliver banking services to many retail and commercial clients and account for well over half of U.S. banking assets.

Profitability for G-SIBs and other large banks exceeded pre-pandemic averages in 2024 and the first half of 2025. These banks benefited from robust fee and trading revenue even as net interest margins (NIM) remained somewhat below long-term trends (see **Figure 4.2.1.5**). G-SIBs and other large banks benefited from a decline in funding costs, but asset yields fell by a similar amount such that NIM improved only marginally.

Delinquency ratios remain low by historical standards despite increasing in recent years due to a deterioration in CRE and consumer credit performance. Robust earnings and the absence of large concentrations in CRE or in the weaker segments of consumer credit (see **Section 4.1.4**) have enabled G-SIBs and large banks to accommodate the necessary allowances for credit loss. Changes to the Federal Financial Institutions Examination Council call report (Call Report) that were introduced in December 2024 and fully implemented in June of 2025 provide new insight into bank lending to non-depository financial institutions (NDFIs). The data shows that NDFI lending by banks stands at about \$1.2 trillion as of the second quarter of 2025 primarily from G-SIBs and other large banks.<sup>115</sup> About 65 percent of that amount is more or less evenly divided between loans to PE funds, business credit intermediaries, and mortgage credit intermediaries. The rest is allocated to consumer credit intermediaries and “other” NDFIs. The new data also indicate that delinquencies on NDFI loans are low.

G-SIBs and other large banks maintain strong risk-based capital positions. Common Equity Tier 1 Capital (CET1) ratios generally fell slightly in the first half of 2025 partially due to growth in risk-weighted assets, but ratios remain near historical highs. The 2025 Federal Reserve Stress Tests, which inform the stress capital buffer, showed that the participating banks have ample capital to withstand a significant economic downturn.

#### Regional Banks

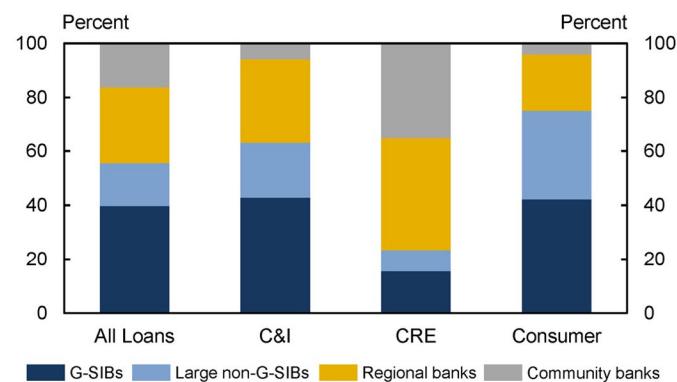
The resilience of regional banks, which have between \$10 billion and \$250 billion in assets, is of paramount importance to the structure and

functioning of the U.S. economy. These banks provide deposits; real estate, consumer, and business loans; and a host of other traditional banking functions. Although smaller than large banks and G-SIBs, regional banks play a significant role in segments such as commercial and industrial, and CRE lending (see **Figure 4.2.1.6**).

As a group, regional banks remain resilient with robust regulatory capital ratios and improvements in liquidity. Different balance sheet characteristics of individual banks have contributed to some divergence in profitability and growth trends among regional banks.

Although regional banks remain somewhat exposed to higher-than-expected interest rates, which could increase refinancing risk and the cost of funding, market trends have generally been beneficial over the past year. For example, unrealized losses in securities portfolios remain elevated by historical standards but have continued to decline. A resumption in deposit growth that started in 2024 after a contraction in 2023 helped regional banks to limit dependence on wholesale funding and lower the cost of deposits. Similarly, there are signs of stabilization in the CRE market, including in the office market and the pockets of the multifamily market that have seen weaker performance (see **Section 4.1.2**). This has enabled banks to reduce some of these exposures, and banks have generally been effective in managing through the challenges associated with CRE concentrations.

#### 4.2.1.6 Loan Distribution by Bank Group



Notes: Data as of 2025:Q2. C&I stands for Commercial & Industrial. CRE stands for Commercial Real Estate.

Sources: FR Y-9C and Call Reports.

#### Community Banks

Although smaller than the other groups of banks, community banks with assets less than \$10 billion play a significant role in the banking system and the nation's economy. By count, community banks represent the vast majority of banks in the United States. By other measures, however, community banks represent a smaller share: in 2025, they had only about 10 percent of total banking industry assets and about 15 percent of total industry loans. Despite holding a small share of total loans, community banks are a key provider of funding to local markets, most importantly by originating CRE loans, residential loans, small business loans, and agricultural loans. For example, community banks originate close to 60 percent of small business loans in the U.S. and about 80 percent of bank-originated agricultural loans.<sup>116</sup>

Community banks continued to report positive financial performance in 2025, including improving return on assets ratios, a widening NIM, and strong asset quality indicators. Leverage ratios at community banks are just above their 10-year averages. The improvement in earnings was widespread with over 75 percent of community banks reporting increases in net income from the prior year when funding cost challenges were more persistent. Robust loan growth, particularly in CRE and residential mortgages in 2025, helped community banks maintain their NIM advantage.

Community banks maintained their margin advantage by earning higher yields on earning assets, which was partly attributable to their holding a higher share of longer-term assets than larger banks. This margin advantage was partially offset by noninterest expense pressures that continued to increase in 2025. Community banks also maintained relatively strong asset quality, limiting the cost of credit losses.

#### Credit Unions

Credit unions are member-owned financial cooperatives with a combined membership of over 143 million Americans. The cooperative business model translates into a concentration of individual members and smaller financial footprints compared to banks. Notwithstanding the 143 million total credit union members nationwide, credit unions are typically not considered a salient threat to financial stability given their relatively small sizes and limited risk-taking.

Consumer lending is the core focus of credit unions. The three major loan types in this category are RRE (roughly 45 percent of total loans), autos (nearly 30 percent of which two-thirds are used vehicles), and credit cards (5 percent). Commercial loans secured by real estate account for just 10 percent of credit union loans, and only a subset of those loans is backed by weaker collateral types (e.g., office buildings).

The credit union industry has faced challenging economic conditions in recent years, such as elevated inflation and higher interest rates, but remains resilient. As of the second quarter of 2025, credit union loan balances had increased 4 percent over the most recent four quarters, signaling a fairly robust credit environment. Insured shares and deposits also increased by 4 percent during that period, bolstering credit union liquidity. The industry's overall delinquency rate (measured as 60-days+ delinquent) stood at 91 basis points in the second quarter of 2025, up moderately from its mid-2024 level of 84 basis points. Profitability has been solid. The industry's NIM was 3.32 percent of average assets in the second quarter, up from 3.05 percent in mid-2024 and the highest level in at least two decades. The credit union industry remains well capitalized, with the system's net worth ratio at 11.11 percent in the second quarter.

#### 4.2.2 Investment Funds

Investment funds, including hedge funds, open-end funds (OEFs), and collective investment funds (CIFs), manage large asset pools and play a key role in facilitating investment and capital formation for businesses, state and local governments, and others. This sector is sizeable, with hedge fund NAVs standing at \$4.5 trillion as of the second quarter of 2025, OEF AUM reaching over \$31.0 trillion as of March 2025, and CIF AUM at \$5.7 trillion as of December 2024.<sup>117</sup> Given the sector's large footprint, investment funds can potentially transmit risk in several ways. For instance, while the hedge fund sector plays a prominent role in liquidity provision, its use of leverage may pose risks in the event of a rapid unwind of leveraged positions during market stress. Further, OEFs have a material presence in several important financial markets, and certain OEFs that offer daily redemptions may be vulnerable to liquidity risk given their investments in less liquid assets, such as certain bonds and bank loans.

#### Hedge Funds

Hedge funds offer individuals and institutions vehicles through which to invest in an array of assets and strategies. Their nimbleness bolsters market efficiency and price discovery. Hedge funds can support financial stability by serving as liquidity providers and can translate information into pricing more rapidly than traditional investors.

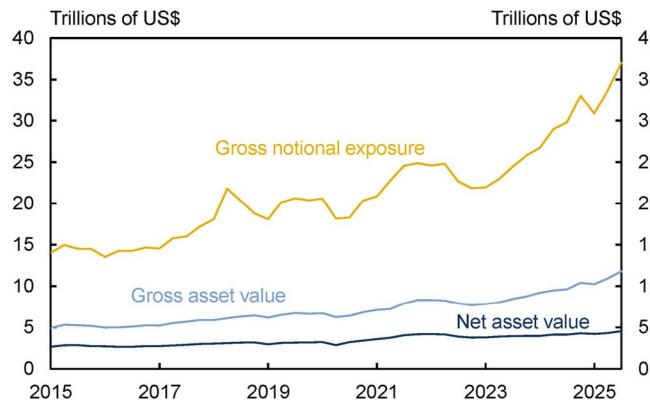
However, hedge funds can also amplify stress in volatile markets. Leverage plays an important role in allowing hedge funds to profit even from small arbitrage opportunities and price discrepancies. While such trades may bolster market efficiency, leverage can increase market risks by magnifying the negative impact of price movements. Indeed, leveraged funds may face pressure to sell to limit losses or meet margin calls in times of stress, exacerbating volatility. Prime brokers and other lenders may, in turn, face losses or engage in procyclical behavior if their counterparties come under pressure. Hedge funds' complexity can make it difficult to evaluate their solvency and risks to other actors during market dislocations.

During 2025, several multi-year trends continued in the hedge fund sector. AUM continued to increase to record levels with growth fueled largely by borrowing. Certain measures of borrower concentration remained elevated, and some liquidity metrics declined for all but the largest funds. Hedge funds' participation in the Treasury market also continued to expand in both the cash and derivatives market segments.

Hedge fund gross assets stood at a record \$11.8 trillion in the second quarter of 2025, up 22.5 percent year-over-year. NAVs also reached a new high of \$4.5 trillion—up 10.0 percent from a year prior—as did gross notional exposure, which hit \$37.0 trillion—up 24.2 percent year-on-year (see **Figure 4.2.2.1**). Since a trough in the third quarter of 2022, gross asset value (GAV) growth has outpaced NAV growth by 2.5x. Much of the hedge fund sectors' growth has therefore come from increased borrowing rather than investor inflows or profits, with secured borrowing standing at \$6.8 trillion at the end of the second quarter of 2025.

Indeed, hedge fund leverage as measured by GAV over NAV averaged a new high of 2.6x at the end of the second quarter of 2025. Leverage is highly

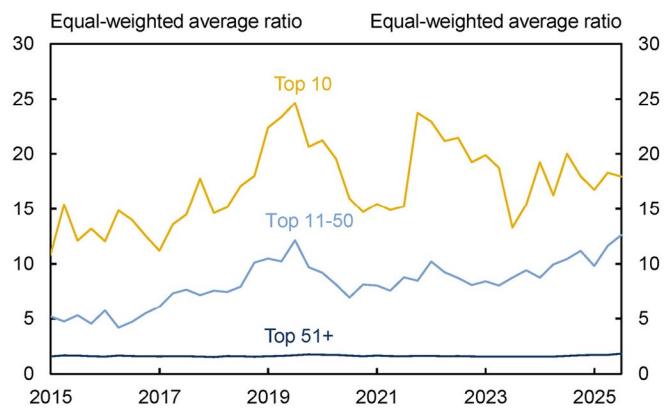
#### 4.2.2.1 Hedge Fund Size



Note: Data as of 2025:Q2.

Source: SEC obtained through the OFR Hedge Fund Monitor.

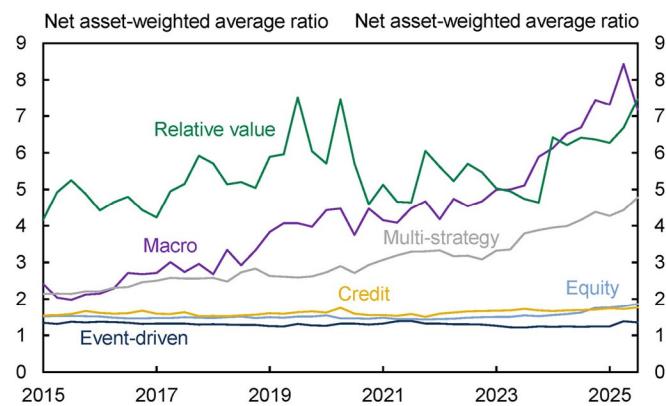
#### 4.2.2.2 Hedge Fund Leverage by Size Cohort



Note: Data as of 2025:Q2.

Source: SEC obtained through the OFR Hedge Fund Monitor.

#### 4.2.2.3 Hedge Fund Leverage by Strategy



Note: Data as of 2025:Q2.

Source: SEC obtained through the OFR Hedge Fund Monitor.

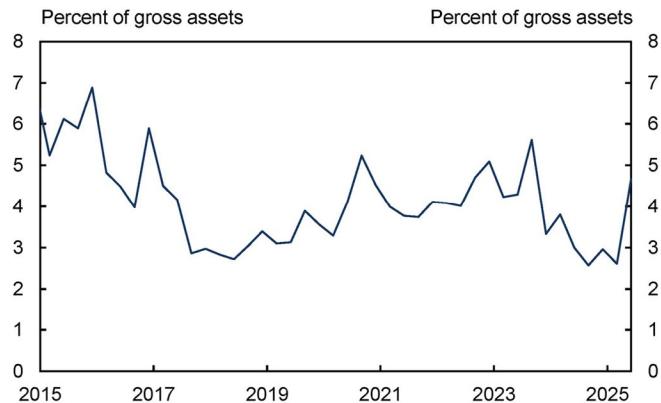
concentrated at the 10 largest funds by GAV (see **Figure 4.2.2.2**), with equal weighted leverage at these 10 funds averaging 18.0x at the end of the second quarter of 2025. Borrowing also remains higher for the top 10 largest funds than it does for their smaller peers. This concentration is noteworthy because challenges at the largest funds could have outsized effects on financial markets and counterparties.

Leverage also varies by strategy. Relative value, macro, and multi-strategy funds remain significantly more leveraged than funds pursuing other strategies with GAV over NAV reaching 7.5x, 7.2x and 4.8x, respectively, in the second quarter of 2025 (see **Figure 4.2.2.3**). Leverage has increased consistently for most fund strategies over the past several years, rising more than 50 percent for macro and multi-strategy funds and 43 percent for relative value funds since the first quarter of 2022.

The extension of credit to leveraged hedge funds is an important channel through which hedge fund conditions can impact broader financial stability. Lending is concentrated with approximately 80 percent of secured lending to hedge funds coming from G-SIBs.<sup>118</sup> Further, three G-SIBs provided more than 40 percent of all secured funding. Creditor concentration, measured by the percentage of borrowing from a fund's three largest creditors, has come down somewhat for the top 10 funds and stood at 49.4 percent at the end of the second quarter 2025, down from 66.4 percent at year-end 2022. Turning to measures of liquidity, unencumbered cash levels for the 10 largest funds by GAV rose over the second quarter of 2025 to 4.7 percent of gross assets from 2.6 percent at the end of the first quarter (see **Figure 4.2.2.4**).

Hedge funds are important participants in and provide meaningful liquidity to U.S. Treasury markets. One example of their participation is the cash-futures basis trade through which hedge funds arbitrage price inefficiencies between cash Treasury and futures markets, as discussed further in **Section 3.1**. The basis trade is beneficial in that it converges prices between futures and cash markets, enhancing Treasury market liquidity and potentially reducing Treasury borrowing costs. As seen in March 2020, however, a rapid unwinding of the basis trade could pose risks if breakdowns in correlations and surges in volatility cause spreads between futures and

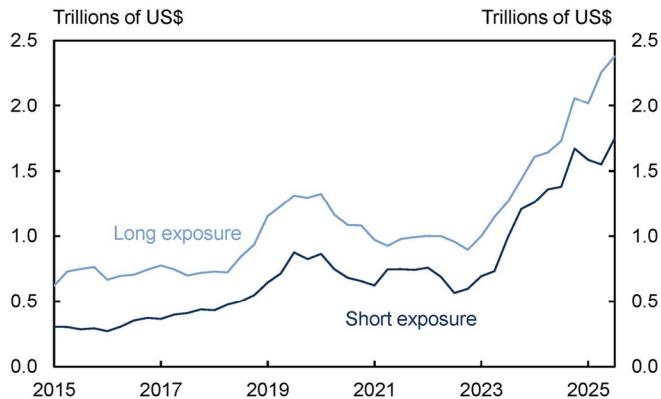
#### 4.2.2.4 Unencumbered Cash Ratios of 10 Largest Funds



Note: Data as of 2025:Q2.

Source: SEC obtained through the OFR Hedge Fund Monitor.

#### 4.2.2.5 Hedge Fund Treasury Exposure



Note: Data as of 2025:Q2.

Source: SEC obtained through the OFR Hedge Fund Monitor.

Treasuries to widen, leading to rapid liquidations to meet margin calls or limit losses, which further exacerbates market volatility.

As discussed in **Section 3.1**, during the April volatility, the basis between cash Treasuries and futures did not widen notably, precluding the need for investors to unwind leveraged basis trade positions as they did in March 2020. The swap market did contribute to volatility as hedge funds positioned for Treasury yield declines unwound positions, putting further upward pressure on yields.

The full size of the basis trade is difficult to quantify, but evidence suggests that it and other relative value Treasury strategies continue to grow. Hedge funds' long U.S. Treasury exposure, which includes both cash and derivatives positions, reached a new high

of \$2.38 trillion as of the second quarter of 2025, which is 88 percent more than the level observed two years earlier. Short exposure also reached a record high at \$1.75 trillion or 77 percent higher than levels from two years earlier (see **Figure 4.2.2.5**). Increasing Treasury exposure tracks the expansion in repo borrowing, which has grown in tandem and reached a record \$3.12 trillion in the second quarter of 2025.

The continued growth of the basis trade and hedge fund borrowing has increased scrutiny of NCCCBR transactions through which hedge funds can borrow against Treasuries inexpensively—in some cases, with low or zero haircuts or margins (see **Section 4.1.1**). Agencies have been considering how implementation of the SEC's central clearing rule may affect any vulnerabilities associated with the basis trade. Supervisors continue to work with banks to improve counterparty credit risk management practices.

#### Open-End Funds<sup>119</sup>

OEFs continue to be large holders of investments in critical markets. These types of funds are a popular and accessible choice for retail investors as they generally offer liquidity, diversification, and transparency. As financial markets have grown more complex, some OEFs are pursuing more complex investment strategies that include investments in less liquid asset classes. To the extent OEFs invest in assets that may not be easily liquidated, a liquidity mismatch may arise between the liquidity offered to shareholders and the relative illiquidity of the fund's portfolio. This mismatch could make it difficult for investors to liquidate their investments without any dilution of the value of the fund's shares. For instance, significant investor outflows from OEFs could lead to an increased volume of underlying asset sales, which, in turn, could stress asset values and lead to large price declines. This could possibly lead to further redemptions and additional distressed asset sales. In times of market stress, this liquidity mismatch could contribute to and amplify stress in the U.S. financial system. To address these challenges, OEFs, including ETFs but excluding MMFs, are required by SEC rule 22e-4 under the Investment Company Act of 1940 to implement a liquidity risk management program designed to ensure that OEFs can meet shareholder redemptions and mitigate shareholder dilution.

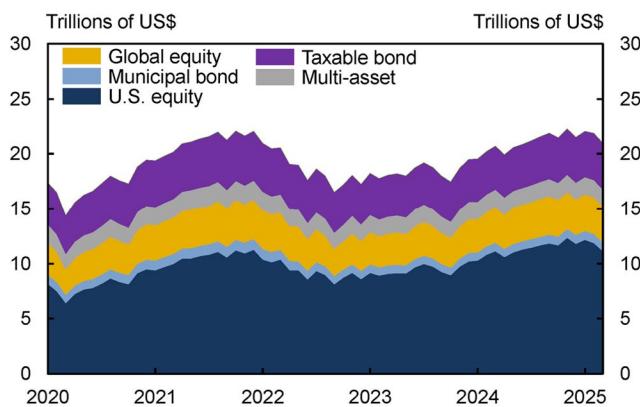
Mutual funds continue to be prominent investors in equity and fixed-income markets, with assets totaling \$21 trillion as of March 2025 (see **Figure 4.2.2.6**), a number that reflects net outflows of approximately \$672 billion during the previous 12 months. Equity-focused mutual funds (global and U.S.) continue to experience sizable outflows, recording \$692 billion in net outflows during this period (see **Figure 4.2.2.7**). Multi-asset funds experienced net outflows totaling \$97 billion while bond mutual funds (taxable and municipal) saw net inflows of \$117 billion for the 12 months ending March 31, 2025.

ETFs have continued to experience rapid growth, partly reflecting investors' interest in shifting assets from mutual funds to ETFs, which typically have lower costs. These can offer greater tax

efficiency and provide intraday liquidity. ETF assets totaled \$10.1 trillion as of March 2025 compared with \$8.6 trillion a year prior (see **Figure 4.2.2.8**). Net inflows into ETFs accounted for \$1.17 trillion of this increase (see **Figure 4.2.2.9**). Net inflows for ETFs focusing on U.S. and global equities totaled \$804 billion, and net inflows for ETFs focusing on bond investments (taxable and municipal) totaled \$354 billion for the twelve months ending March 31, 2025. Leveraged and inverse ETFs had total assets of \$153 billion as of September 2025, accounting for less than 2 percent of total ETF AUM.

Over the 12-month period ending March 31, 2025, index funds (generally, passively managed mutual funds and ETFs) had net inflows of \$849 billion while non-index funds (generally, actively

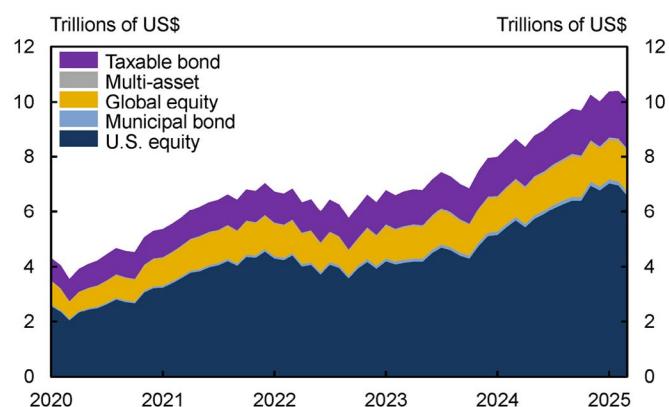
#### 4.2.2.6 Mutual Fund AUM



Note: Data as of March 2025.

Source: SEC.

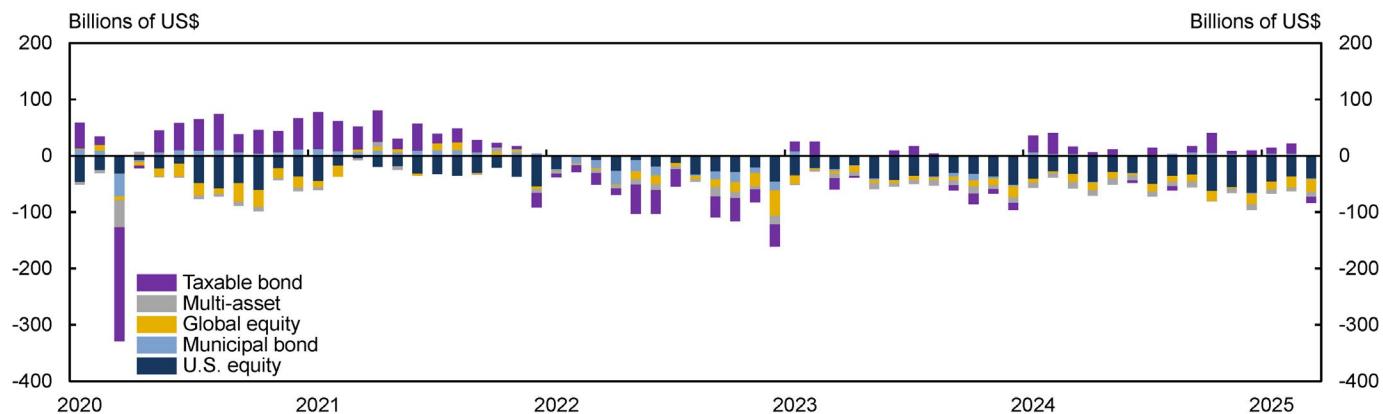
#### 4.2.2.8 ETF AUM



Note: Data as of March 2025.

Source: SEC.

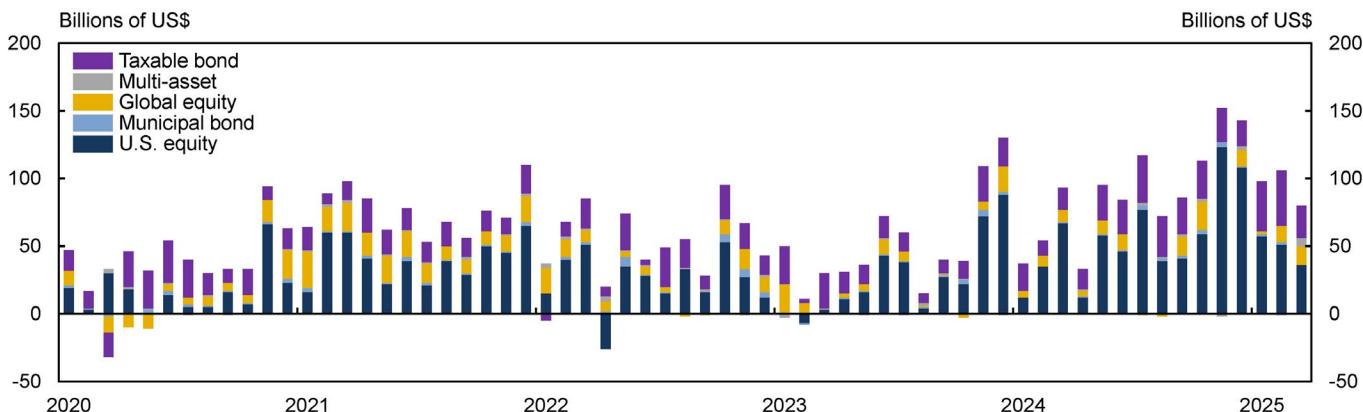
#### 4.2.2.7 Mutual Fund Net Flows



Note: Data as of March 2025.

Source: SEC.

#### 4.2.2.9 ETF Net Flows



Note: Data as of March 2025.

Source: SEC.

managed mutual funds and ETFs) had net outflows of \$350 billion. As of March 2025, such index funds had total assets of \$16.3 trillion while such non-index funds had total assets of \$16.1 trillion.

In August 2024, the SEC adopted amendments to reporting requirements for Form N-PORT, which details portfolio holdings of many registered investment companies. The amendments require timely information about funds' portfolio investments. In April 2025, the SEC delayed the effective and compliance dates of these amendments in accordance with the 2025 Presidential Memorandum, "Regulatory Freeze Pending Review," and anticipates determining whether further amendments or revisions to the adoption are necessary.<sup>120</sup>

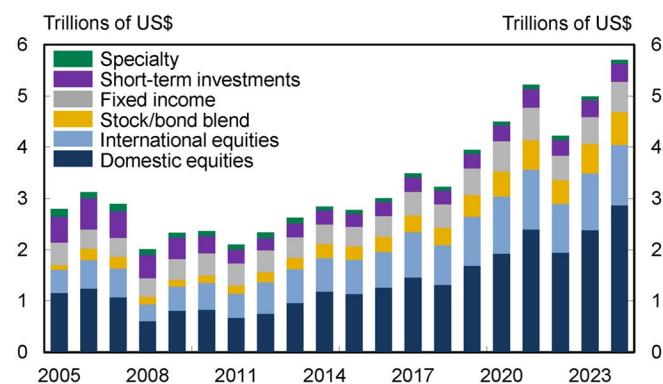
#### Collective Investment Funds

CIFs are bank- and trust company-administered funds that hold pooled assets of eligible fiduciary accounts. CIFs generally comprise common trust funds for accounts for which the bank acts as trustee and collective investment trusts offered to tax-exempt qualified retirement plans. CIFs are pooled investment vehicles that are collectively managed in accordance with a specified investment strategy.

Certain CIFs may present liquidity, leverage, and investment risks, as well as financial stability risks. However, several factors may mitigate the risks that CIFs pose, including limitations on eligible investors. Additionally, CIFs have flexibility in terms of withdrawals, including by offering notice periods, setting withdrawal dates, or restricting withdrawals.

While individual federal and state regulators collect varying degrees of data on the CIF activities of the banks and trust companies they supervise, not all of these data are publicly available. Therefore, the Council has limited data on the size and holdings of the entire CIF industry. Banks and trust companies filing Call Reports reported over \$5.7 trillion in CIF AUM as of year-end 2024 as compared to \$5.0 trillion as of year-end 2023 (see **Figure 4.2.2.10**).<sup>121</sup> The growth in CIF AUM reflects market appreciation, as well as new investments by eligible investors. For example, qualified retirement plans have expanded their investments in CIFs in part due to their low operating expenses, negotiable fee structures, and flexible investment opportunities.

#### 4.2.2.10 Collective Investment Fund AUM by Sector



Notes: Data as of 2024. Chart shows only funds managed by institutions reporting CIF and CIT assets on Call Report Schedule RC-T.

Source: Call Reports.

#### **4.2.3 Central Counterparties**

CCPs act as key nodes within the global financial system by providing central clearing services. Central clearing involves the creation of two matched contracts wherein the CCP acts as buyer to every seller and seller to every buyer. Under Title VIII of the Dodd-Frank Act, the Council has designated five CCPs as systemically important financial market utilities: the Chicago Mercantile Exchange (CME), FICC, the National Securities Clearing Corporation (NSCC), ICE Clear Credit, and the Options Clearing Corporation. These designations are due to the potential impact on financial stability if these CCPs were to fail or experience disruptions in their functioning.

CCPs offer several benefits from a financial stability perspective including robust risk management practices. An integral aspect of a CCP's risk management involves the collateralization of open contracts through the collection of initial and variation margin. Initial margin is used to support contract performance should a clearing member fail to fulfill its obligations to the CCP. CCPs can adapt initial margin requirements in response to shifts in market dynamics, which may cause CCPs to increase these margin requirements during periods of market volatility. Further, CCPs conduct mark-to-market valuations on all cleared positions at least daily and facilitate the exchange of variation margin payments. The amount of variation margin exchanged can also increase during periods of market volatility. During such periods, CCPs may call for additional margin on an intraday basis.

CCPs collect additional prefunded resources to cover potential losses associated with the default of a clearing member and have specific, predefined default procedures in place to close out a defaulter's positions and allocate losses. Another key benefit of central clearing is multilateral netting that allows for offsetting trades cleared through the CCP to be margined and settled on a net basis. This can reduce the risk of settlement failures as well as the amount of initial and variation margin collected.

As discussed above, CCPs offer advantages in terms of robust risk management and market efficiency; however, they also carry unique vulnerabilities. For example, the inability of a CCP to meet its obligations stemming from either the default of one or more clearing members or losses due to operational failures has the potential to strain both

the remaining CCP members and, on a broader scale, the entire U.S. financial system. Efficiencies from netting within the same CCP incentivizes the concentration of clearing services for similar product types, leading to CCPs playing a critical role in the markets they clear. Clearing members are also highly concentrated. The same 10 G-SIBs are clearing members at the same global CCPs, and broadly, the top 10 clearing members cleared over 80 percent of client transactions across several U.S.-based CCPs.<sup>122</sup>

This concentration may heighten liquidity and operational risk among others. For instance, as noted above, CCPs can require additional resources from clearing members through margin calls, including intraday margin calls, during periods of market volatility. These calls may place liquidity demands on clearing members especially during periods of market volatility that can cause a CCP's risk management to have a procyclical impact and amplify potential liquidity strains in the event of a shock. Further, the failure of a common, large clearing member could result in simultaneous default processes at several CCPs. Although CCPs collect prefunded resources to manage the default of one or more clearing members, if these resources prove insufficient, clearing members may face concurrent portfolio auctions or additional assessments, which may stress non-defaulting clearing members and transmit instability to the broader financial system. Lastly, as CCPs are central nodes in the financial system, service disruptions or losses due to operational incidents can also have adverse impacts on clearing members and clients and result in stress to financial markets more broadly.

#### **CCP-Related Market Developments**

Over the past year, levels of prefunded resources at CCPs and volumes across centrally cleared markets remained elevated by historical standards. Increased volumes were especially evident during the April volatility, although CCPs operated without major incident during that period.

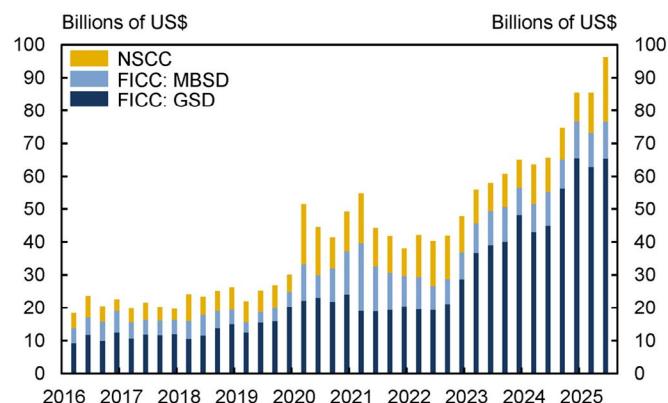
In the cash securities markets, clearing fund requirements across the three clearing services of the Depository Trust and Clearing Corporation (DTCC) stood at all-time highs. This was driven by FICC's government securities division (GSD) in response to trends in the size of the Treasury market

and partial movement from firms ahead of the expansion of Treasury central clearing.<sup>123</sup> DTCC's aggregate clearing fund requirements totaled \$96.3 billion as of June 30, 2025, up \$30.7 billion from June 28, 2024 (see **Figure 4.2.3.1**). Further, initial margin posted against exchange-traded derivatives at CME, Options Clearing Corporation, and ICE Clear U.S. was elevated, with initial margin totaling \$417 billion as of the second quarter of 2025 (see **Figure 4.2.3.2**). Of note, equities futures experienced substantial volatility in the second quarter of 2025. From April 2, 2025 to May 12, 2025, initial margin requirements on futures contracts for the Standard and Poor's 500 (S&P 500) rose over 37 percent per contract. However, as noted above, no major incidents were reported.

The absolute level of initial margin for over-the-counter (OTC) derivatives rose to \$364 billion, with \$94 billion contributed to domestic CCPs as of June 30, 2025, up \$49 billion from the prior June (see **Figure 4.2.3.3**). As in 2024, initial margin levels for interest rate swaps remained elevated this year with most of the increase attributable to interest rate volatility as central banks maintained higher target rates than in prior years.

Across U.S. CCPs, operational disruptions returned to historical averages compared to lows observed in 2024 despite heterogeneity among clearing houses (see **Figure 4.2.3.4**). Some CCPs have experienced more incidents and longer operational failures; nevertheless, these CCPs have maintained availability for critical services in excess of 99 percent.

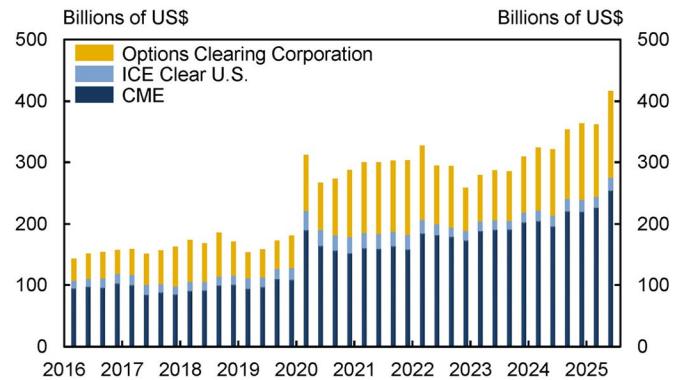
#### 4.2.3.1 DTCC Clearing Fund Requirements



Note: Data as of 2025:Q2.

Source: PFMI Quantitative Disclosures (Clarus Financial Technology, 4.1.4).

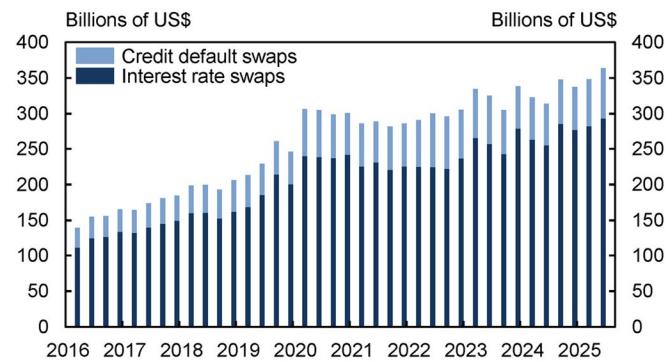
#### 4.2.3.2 Initial Margin: U.S. Exchange-Traded Derivatives



Notes: Data as of 2025:Q2. Bars show initial margin required as reported in quantitative disclosures, including house and client accounts.

Source: PFMI Quantitative Disclosures (Clarus Financial Technology, 6.1.1).

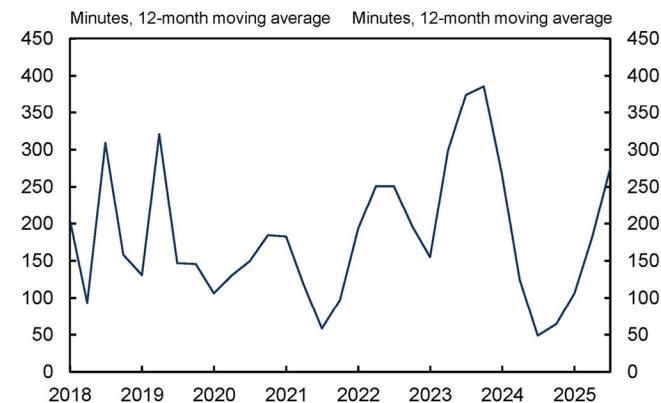
#### 4.2.3.3 Initial Margin: Centrally Cleared OTC Derivatives



Notes: Data as of 2025:Q2. Bars show initial margin required as reported in quantitative disclosures, including house and client accounts. Interest rate swaps margin includes LCH Ltd. and CME. Credit default swaps margin includes CME, ICE Clear Credit (ICC), ICE Clear Europe (ICEU), and LCH SA. CME and ICEU ceased clearing CDS in March 2018 and October 2023, respectively.

Source: PFMI Quantitative Disclosures (Clarus Financial Technology, 6.1.1).

#### 4.2.3.4 Average Time of U.S. CCP Operational Disruptions



Note: Data as of 2025:Q2.

Source: PFMI Quantitative Disclosures (Clarus Financial Technology, 17.3).

## Regulatory Developments

### Expansion of Treasury Clearing

The SEC has adopted rules that, once implemented, will expand the central clearing of U.S. Treasury securities and repo transactions. The compliance dates for clearing under these rules, as modified in February 2025, are December 31, 2026, for cash Treasuries, and June 30, 2027, for Treasury repo and reverse repo. Additional central clearing of the Treasury market will encourage more standardized risk-management practices across market segments including more uniform margining practices, potentially improving the resilience of the Treasury market. See **Section 3.1** for additional discussion of expanded Treasury central clearing.

In addition to FICC, the sole CCP currently offering U.S. Treasury clearing, several CCPs have announced their intention to provide clearing services for U.S. Treasuries since the adoption of the rule. CME, through a new entity CME Securities Clearing, Inc., was approved to clear cash Treasury securities and repos on December 1, 2025.<sup>124</sup> ICE, through the existing entity ICE Clear Credit LLC, has formally applied to do so.<sup>125</sup>

In general, CCPs benefit from economies of scale and network effects, which naturally lead CCPs to become highly concentrated. Multiple CCPs clearing the same product may both amplify and mitigate financial stability risks depending on the circumstances. In terms of operational risks, multiple CCPs clearing the same products generate redundancy in the event of a large-scale operational failure at a single CCP. With regard to margining, multiple CCPs could result in increased and potentially inefficient margining due to a reduction in netting if clearing member positions are spread across CCPs. Liquidation costs may also be more difficult to assess because of the use of different liquidation strategies, agents, and participants. While current margin and liquidity requirements may ameliorate some of these concerns, the broader implications for financial stability will need to be evaluated.

### Operational Risk

Robust management of operational risk, either due to cyber attacks or due to operational disruptions, is particularly relevant for CCPs due to their role as central nodes within the financial sector. International standards, such as the *Principles for*

*Financial Market Infrastructures*, state that CCPs and other financial market infrastructures should identify the plausible sources of operational risk, both internal and external, and mitigate their impact through the use of appropriate systems, policies, procedures, and controls.<sup>126</sup>

These principles have been implemented by national regulators through rulemaking designed to introduce operational resilience standards. Further, market participants have worked on cyber coordination via the FSSCC and the Financial Services Information Sharing and Analysis Center, among other groups. Relevant authorities are attentive to operational risks that CCPs face and continue to consider practices to enhance operational resilience and address non-default losses (NDLs).

### Resolution Planning

Systemically important CCPs have taken measures overseen by regulators to bolster their preparedness to manage extreme stress scenarios, such as engaging in recovery and orderly wind-down planning to support market functioning should a CCP become impaired. A CCP's inability to recover or wind down in an orderly manner could create serious financial stability concerns. While historical instances of CCP failures have been infrequent, the impact of a potential CCP failure demands thorough resolution planning and readiness by relevant authorities to ensure the continuous operation of essential functions and preservation of U.S. financial stability.

To enhance the readiness of authorities in a potential resolution event, it is important for relevant authorities to coordinate before a resolution is required. Coordination requires access to appropriate resources, a clear understanding of relevant authorities' roles, and timely information sharing amongst authorities with respect to participants and market developments so that authorities are prepared to take appropriate actions should resolution be required. Relevant authorities in the U.S. continue to work collectively to establish the required systems and capabilities for any appropriate actions.

### 4.2.4 Insurers

The U.S. insurance sector is sizeable, holding approximately \$12.3 trillion in invested assets as

of the second quarter of 2025. Within the sector, life insurers hold approximately 75 percent of those assets, or \$9.2 trillion, with property and casualty (P&C) insurers holding the remaining 25 percent, or \$3.1 trillion.<sup>127</sup> Given insurers' large footprint, they are significant asset holders in many important markets, including corporate bonds and commercial mortgages, and have increasing interconnections within the broader financial system. Further, the life insurance sector continues to evolve due to a number of structural shifts and new market participants. Meanwhile, in the P&C sector, property owners continue to face challenges related to cost and availability of coverage in certain regions. As insurance is regulated at the state level, the Council supports work by the state insurance regulators to monitor and evaluate the potential impacts of these structural changes, including the growing use of offshore reinsurance, increasing allocation in insurers' investment portfolios to nontraditional assets, the increasing role of private credit, and any associated implications for financial stability.

### Life Insurers

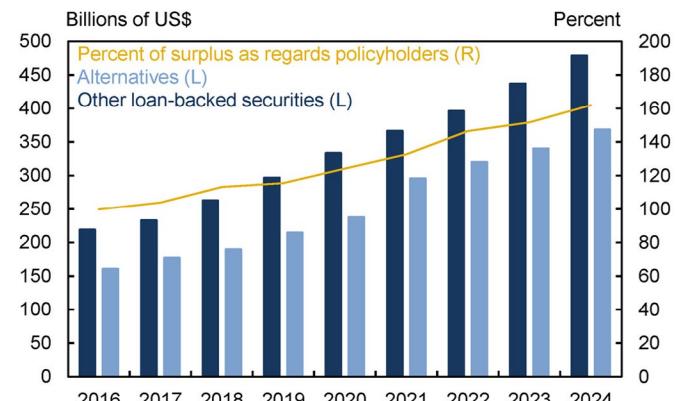
As noted, the life insurance sector makes up the majority of insurer assets and has continued to experience a number of important structural changes, including increasing exposure to nontraditional asset classes, increasing ownership by alternative asset managers, shifts in the composition of liabilities, and further growth in the use of offshore reinsurance. Accordingly, such market developments and increased interconnections with the broader financial system suggest the need for close monitoring by state regulators given implications for the sector.

Overall, life insurer general account assets have maintained consistent growth, averaging a 4.8 percent annual rate over the past five years and total investment holdings have expanded at an annual rate of 4.6 percent on average during the same period. The sector's investment portfolio growth during 2024 was primarily driven by increased holdings of mortgage loans, residential MBS, and other loan-backed structured securities. Additionally, investment in CRE loans increased about 2.6 percent in 2024.<sup>128</sup> As commercial mortgage loan cash flows align with long-dated liabilities and produce attractive yields, life insurers generally have significant commercial

mortgage loan exposures. Overall, life insurers appear to generally have well-diversified real estate exposure and a sufficient capital cushion to absorb potential losses.<sup>129</sup>

Further, life insurers continue to increase allocations to alternative and other nontraditional asset classes. Today, insurers hold private credit loans and asset-backed securities (including middle market CLO tranches) on their balance sheets, invest in PE and private credit funds as limited partners, and provide credit facilities to private funds. As shown in **Figure 4.2.4.1**, insurer holdings of these assets have steadily increased since 2016. Indeed, life insurer holdings of alternatives stood near \$368 billion as of 2024, up approximately 130 percent from 2016.

#### 4.2.4.1 Life Insurers' Changing Investment Portfolios



Note: Data as of 2024.

Source: S&P Global Market Intelligence LLC.

PE ownership of life insurers has been a growing trend over the last decade. The number of PE-owned U.S. insurers identified by the NAIC was 139 as of June 2025 compared to 90 as of December 2019.<sup>130</sup> Based on year-end 2024 NAIC annual statement filings, total cash and invested assets for the 137 PE-owned insurers at year-end 2024 increased about 16 percent to \$704.3 billion, representing 7.8 percent of all U.S. insurers' total cash and invested assets, compared to 7.1 percent in 2023. The primary focus of state regulators has centered on those investment activities and products that cause concern rather than focusing on any particular ownership structure.

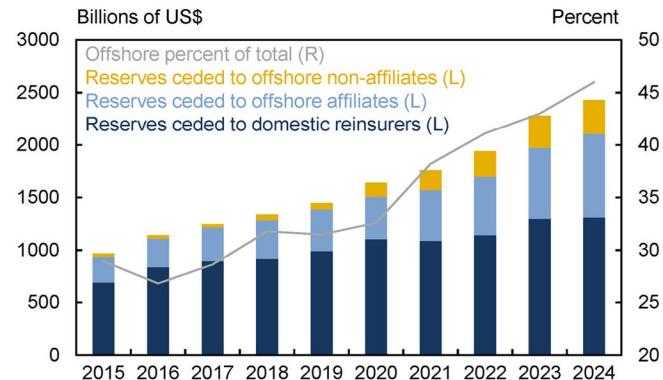
Life insurers also continue to rely on nontraditional funding sources, such as spread-

based products, which include issuance of funding agreements that are subsequently packaged into funding agreement backed notes (FABNs) for institutional investors. These products are not treated as debt in statutory accounting, which allows life insurers to exclude them from certain measures of leverage. Despite potential diversification of funding sources, how features and market practices of these products may impact liquidity risk warrants monitoring. Advances from the Federal Home Loan Bank (FHLB) system represent another source of nontraditional funding. Advances to insurers continued to increase in 2025, growing 13 percent year-on-year to \$175 billion as of the second quarter 2025.<sup>131</sup> FHLB advances offer insurers several benefits, including favorable treatment from credit rating agencies and a source of low-cost funding. In addition, FHLB advances can serve as an important source of short-term funding in times of need as insurers lack a lender of last resort. In terms of traditional products, overall annuity sales reached record highs in 2024, surpassing \$430 billion.<sup>132</sup> However, as short-term interest rates began to decline in the second half of 2024, sales of fixed rate annuities have tempered after several years of rapid growth.

Further, the use of reinsurance, particularly from offshore jurisdictions, has continued to increase. The amount of reserves that U.S. life insurers have ceded to reinsurers increased by over 70 percent since 2019, rising to \$2.4 trillion in 2024 from \$1.4 trillion. Over that same period, reserves ceded to offshore jurisdictions more than doubled and exceeded \$1.1 trillion (see **Figure 4.2.4.2**). Currently, most U.S. reserves ceded to offshore reinsurers go to reinsurers domiciled in Bermuda with an increasing amount of reserves being ceded to Cayman Islands reinsurers. Additionally, nearly 70 percent of life and annuity reserves ceded offshore go to affiliated reinsurers, and insurers with asset manager or PE sponsors comprise 46 percent of reserves ceded to such offshore affiliates.<sup>133</sup> Such affiliated arrangements may introduce additional opacity and complexity.

Regulation and supervision of the life insurance sector by state insurance regulators has evolved in response to these trends while some questions remain regarding the impact of different regulatory, accounting, and tax regimes, as well as counterparty risk exposures. State insurance

#### 4.2.4.2 More Life Insurance Reserves Are Moving Offshore



Notes: Data as of 2024. Reserves ceded to domestic reinsurers includes U.S. affiliated and unaffiliated.

Source: NAIC.

regulators are also exploring enhancements to stress testing, investment and product disclosures, and analysis of collateral suitability to ensure reserves are adequate to support life insurers' obligations.

#### Property and Casualty Insurers

The P&C insurance sector's invested assets reached nearly \$3.1 trillion as of the second quarter of 2025, and net premiums written reached \$935 billion in 2024, reflecting 8 percent growth over the last year.<sup>134</sup> Premium growth in both personal lines (e.g., personal auto and homeowners) and commercial lines (e.g., commercial multi-peril) were driven by both general growth in the domestic economy and rate increases. Despite higher estimated insured catastrophic losses, the general impacts of regulatory constraints, inflationary pressures, and rising reinsurance costs during 2024, the sector experienced a sharp increase in underwriting profit and net income. Net income was also boosted by increases in net investment income and net realized capital gains.

For the U.S. P&C insurance sector in 2024, liquidity levels continued to rise, as insurers slightly pulled back from riskier assets and experienced strong premium growth. P&C insurers implemented premium rate increases in 2023 and 2024 to address inflationary pressures, higher natural catastrophe losses, and other loss and expense concerns. Net premiums earned grew by nearly 10 percent for the second consecutive year as a result, which supported increased earnings and liquidity for the sector.

Within the P&C insurance sector, residential property insurance continues to attract attention as property owners in certain areas experience challenges finding and affording insurance. In 2024, insurers continued to raise rates or pull back from writing policies in certain areas in response to rising insured losses and other factors. National average homeowners insurance premiums increased 10.4 percent in 2024 while average rates of policy nonrenewals rose from 1.08 percent to 1.58 percent.<sup>135</sup>

Commercial policies written for condominiums, cooperative apartments, homeowners associations, and multifamily rental properties also experienced more restrictive terms, tightened underwriting requirements, and increased prices driven by factors broadly affecting homeowners insurance, as well as by underwriting and regulatory changes made in response to the deadly Surfside Condominium collapse in 2021.

In some cases, difficulty securing adequate insurance at the master policy level has made it more difficult for owners to sell individual condominiums. Such availability and affordability challenges can place pressure on states that have residual markets, which serve as the “insurers of last resort” in the District of Columbia and the 34 states in which they have been established. Between 2019 and 2024, the total number of residential policies in residual markets increased 77 percent to 3.2 million policies, with the growth primarily in five states: California, Florida, Louisiana, North Carolina, and Texas; relatively smaller increases occurred in three other states (Alabama, Oregon, and Washington), while the number of residential policies in other states’ residual market plans declined.<sup>136</sup> Homeownership costs, including the cost of insurance, may influence the value of homes, which is the largest financial asset for many Americans.

# Section 5. Council Activities and Regulatory Developments

## 5.1 Council Activities

### 5.1.1 Risk Monitoring and Regulatory Coordination

The Dodd-Frank Act charges the Council with the responsibility to identify risks to U.S. financial stability, promote market discipline, and respond to emerging threats to the stability of the U.S. financial system. The Council also has a duty to facilitate information sharing and coordination among member agencies and other federal and state agencies regarding financial services policy and other developments.

Over this past year, Council member agencies have monitored risks and coordinated through the Council's Systemic Risk Committee (SRC) and FMU Committee.

The SRC supports the Council's efforts in identifying risks and responding to emerging threats to the stability of the U.S. financial system. The committee serves as a forum for all member agencies to convene, facilitate information sharing on recent market events, and monitor developments within financial markets. The committee's analysis of financial markets and institutions over the past year has informed the Council's assessment of these issues in this Report.

The FMU Committee serves as a forum to identify and monitor potential threats or risks to U.S. financial stability that could be related to or mitigated through financial market utility, payment, clearing, and settlement activities. Over the last year, the committee has focused on issues related to crisis preparedness at critical market infrastructure and has monitored the implementation of the expansion of central clearing for U.S. Treasury securities and repo transactions.

### 5.1.2 Determinations Regarding Nonbank Financial Companies

One of the Council's statutory authorities is to determine that a nonbank financial company

will be subject to enhanced prudential standards and supervision by the Federal Reserve if material financial distress at the company, or if the nature, scope, size, scale, concentration, interconnectedness, or mix of activities of the company could pose a threat to U.S. financial stability. The Dodd-Frank Act sets forth the standard for the Council's determinations regarding nonbank financial companies, and it requires the Council to evaluate ten specific considerations and any other risk-related factors that the Council deems appropriate when evaluating those companies.

As of the date of this report, no nonbank financial companies are subject to a final determination by the Council under Section 113 of the Dodd-Frank Act or are under review in Stage 1 or Stage 2 of the Council's designation process. The Council intends to review its guidance related to nonbank financial company determinations under Section 113 of the Dodd-Frank Act and the Council's analytic framework for financial stability risks.

### 5.1.3 Operations of the Council

The Dodd-Frank Act requires the Council to convene no less frequently than quarterly. The Council held four meetings in 2025, one in each quarter. The meetings bring Council members together to discuss and analyze market developments, potential threats to financial stability, and financial regulatory issues. Although the Council's work frequently involves confidential supervisory and sensitive information, the Council is committed to conducting its business as openly and transparently as practicable. Consistent with the Council's transparency policy, the Council opens its meetings to the public whenever possible. The Council held a public session at two of its meetings in 2025. Approximately every two weeks, the Council's Deputies Committee, composed of senior representatives of Council members, convenes to discuss the Council's agenda and to coordinate and oversee the work of the Council's other staff-level committees. The Council adopted its fiscal year 2026 budget in September 2025.

## 5.2 Safety and Soundness

### 5.2.1 Enhanced Capital and Prudential Standards and Supervision

On March 14, 2025, the FDIC withdrew three notices of proposed rulemaking relating to brokered deposit restrictions, corporate governance and risk management, and the Change in Bank Control Act. These proposed rules would have revised regulations related to brokered deposits and disrupted many aspects of the deposit landscape, established new safety and soundness standards consisting of prescriptive and process-oriented expectations rather than focusing on core safety and soundness risks, and required a range of bank investors to file duplicative notices to both the FDIC and Federal Reserve System and could have discouraged capital investments.

On July 3, 2025, the FDIC rescinded the 2024 Statement of Policy on Bank Merger Transactions and reinstated its pre-2024 Statement of Policy. The 2024 Statement of Policy added considerable uncertainty to the merger application process and raised additional questions regarding when merger applications would be required.

On July 28, 2025, the FDIC issued a notice of proposed rulemaking that would amend certain regulatory thresholds in the FDIC's regulations to reflect inflation. Specifically, the proposal would generally update such thresholds to reflect inflation from the date of initial implementation or the most recent adjustment and provide for future adjustments pursuant to an indexing methodology. The changes set forth in the proposal would provide a more durable regulatory framework by helping to preserve, in real terms, the level of certain thresholds set forth in the FDIC's regulations, thereby avoiding the undesirable and unintended outcome where the scope of applicability for a regulatory requirement changes due solely to inflation rather than actual changes in an institution's size, risk profile, or level of complexity.

On October 6, 2025, the OCC reduced the supervisory burden for community banks by updating its policies effective January 1, 2026, to eliminate certain examination activities not required by statute or regulation. As an additional burden reduction for community banks, the OCC also announced it will examine retail nondeposit

investment products (RNDIPs) at community banks under OCC core assessment standards for community bank supervision and not under specialized RNDIP examination processes that are generally unsuitable for community banks.

On October 6, 2025, the OCC issued a notice of proposed rulemaking to simplify licensing requirements for corporate activities and transactions involving national banks and Federal savings associations that have less than \$30 billion in total assets and that satisfy certain conditions. On October 7, 2025, the FDIC and OCC issued a joint notice of proposed rulemaking on unsafe or unsound practices and the supervisory framework for the issuance of Matters Requiring Attention (MRAs). The proposal would establish a uniform definition for the term "unsafe or unsound practice" for purposes of the agencies' enforcement and supervisory authorities. The proposal would also establish uniform standards for when and how the agencies communicate MRAs and nonbinding supervisory observations as part of the examination process.

On October 7, 2025, the FDIC and OCC also issued a joint notice of proposed rulemaking on the use of reputation risk, which would codify the removal of reputational risk from the agencies' supervisory programs.

On October 16, 2025, the OCC, Federal Reserve, and FDIC rescinded the October 30, 2023, Principles for Climate-Related Financial Risk Management. In the context of existing safety and soundness standards, the agencies were concerned these principles could distract from management of other potential risks.

On November 17, 2025, the Federal Reserve adopted a final notice to revise its LFI rating system (LFI Framework) and the rating system for depository institution holding companies significantly engaged in insurance activities (Insurance Supervisory Framework, together with the LFI Framework, Frameworks) to more appropriately identify as "well managed" firms that have sufficient financial and operational strength and resilience to maintain safe and sound operations through a range of conditions, including stressful ones. The final notice also replaces the presumption in the Frameworks that firms with one or more Deficient-1 component ratings will be subject to a formal or

informal enforcement action with a statement that such firms may be subject to a formal or informal enforcement action, depending on particular facts and circumstances. The final notice also removes a reference to reputational risk in the Insurance Supervisory Framework.

On November 25, 2025, the Federal Reserve, FDIC, and OCC finalized a rulemaking to modify the eSLR standards applicable to U.S. bank holding companies identified as G-SIBs and their depository institution subsidiaries.<sup>137</sup> Specifically, the rulemaking modifies the eSLR buffer standard applicable to G-SIBs to equal 50 percent of the bank holding company's method 1 surcharge as determined by the Federal Reserve's G-SIB risk-based capital surcharge framework. The rule also modifies the eSLR standard for covered depository institutions to have the same form and calibration as the G-SIB standard, subject to a maximum leverage buffer of 1 percent. The modifications will help ensure that the eSLR standards serve as a backstop to risk-based capital requirements rather than as a constraint that is frequently binding over time and through most points in the economic and credit cycle, thus reducing potential disincentives for G-SIBs and their depository institution subsidiaries to participate in low-risk, low-return businesses. The Federal Reserve also finalized amendments to its total loss-absorbing capacity and long-term debt requirements to maintain alignment between these requirements and the eSLR standards. The Federal Reserve also made conforming amendments to relevant regulatory reporting forms. The Federal Reserve and FDIC also made certain technical corrections to the capital rule.

On November 25, 2025, the Federal Reserve, FDIC and OCC issued a notice of proposed rulemaking that would modify the CBLR framework. The proposal would lower the CBLR requirement for certain depository institutions and depository institution holding companies from 9 percent to 8 percent, consistent with the lower bound provided in Section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. The proposal would also extend the length of time that certain depository institutions or depository institution holding companies can remain in the CBLR framework while not meeting all of the qualifying criteria for the CBLR framework from two quarters to four quarters, subject to a limit of eight

quarters in any five-year period. The proposed modifications are intended to encourage broader adoption of the CBLR.

### **5.2.2 Dodd-Frank Act Stress Tests**

On April 22, 2025, the Federal Reserve issued a notice of proposed rulemaking that would amend the calculation of the Federal Reserve's stress capital buffer requirement applicable to certain large bank holding companies, savings and loan holding companies, U.S. intermediate holding companies of foreign banking organizations, and nonbank financial companies supervised by the Federal Reserve to reduce the volatility of the stress capital buffer requirement. The proposal would use the average of the maximum CET1 declines projected in each of the Federal Reserve's prior two annual supervisory stress tests to inform a firm's stress capital buffer requirement. The proposal would also extend the annual effective date of the stress capital buffer requirement by one quarter to January 1 to provide additional time for firms to comply with the requirement. In addition, the proposal would make changes to the FR Y-14A/Q/M reports to collect additional net income data that would improve the accuracy of the stress capital buffer requirement calculation, as well as remove data items that are no longer needed to conduct the supervisory stress test. The changes in the proposal are not designed to materially affect overall capital requirements and would decrease regulatory reporting burden.

On October 24, 2025, the Federal Reserve issued a notice of proposed rulemaking focused on enhancing the transparency and public accountability of its annual stress test. The proposal would amend the Policy Statement on the Scenario Design Framework for Stress Testing, including to implement guides for additional scenario variables, and the Stress Testing Policy Statement. The proposal would also codify an enhanced disclosure process under which the Federal Reserve would annually publish comprehensive documentation on the stress test models, invite public comment on any material changes that the Federal Reserve seeks to make to those models, and annually publish the stress test scenarios for comment. Lastly, the proposal would make changes to the FR Y-14A/Q/M to remove items that are no longer needed to conduct the supervisory stress test and to collect additional data to support the stress test models and improve risk capture.

### **5.2.3 Resolution Planning and Orderly Liquidation**

On April 18, 2025, the FDIC modified its approach to resolution planning for large banks and exempted insured depository institutions (IDIs) from certain content requirements of the IDI Rule, such as requirements to utilize a bridge bank strategy and a hypothetical failure scenario in the plan. This approach focuses IDI resolution planning processes on the most relevant operational information for the FDIC. The FDIC also issued an updated set of frequently asked questions describing the exemptions and clarifying certain expectations.

### **5.2.4 Insurance**

FIO assists the Secretary of the Treasury in administering the Terrorism Risk Insurance Program (TRIP), created under the Terrorism Risk Insurance Act of 2022, as amended. In June 2025, Treasury published a Study of Small Insurer Competitiveness in the Terrorism Risk Insurance Marketplace. In addition to providing updates on the role of small insurers in the terrorism insurance marketplace, the report provides insights on the cyber insurance market in the TRIP-eligible lines of insurance. The report also shares analysis based upon terrorism risk models to evaluate potential impacts on small insurers under TRIP. The report finds that small insurers are important components of the large and diverse U.S. insurance market and are also significant participants in the market for terrorism risk insurance in the United States. The report finds that small insurers' market share of TRIP-eligible lines of insurance has been stable since 2017 with numerous market differences between small and large insurers.

On May 2, 2025, FIO hosted a roundtable discussion with representatives from the insurance sector, including insurers, reinsurers, brokers, state regulators, resilience and consumer groups, and academics to discuss ways to lower costs and maintain availability of homeowners insurance as part of the Administration's efforts to address the cost-of-living crisis. Senior Treasury officials led discussions on cost and availability issues within the homeowners insurance market as well as current efforts by the insurance sector, state and local governments, and regulators to address these issues.

FIO participated in the President's Working Group on Digital Asset Markets and contributed to the Digital Assets Report, which includes a section on insurance and digital assets. The report includes various steps Treasury and state regulators could take to help improve regulatory certainty and develop a more robust market for digital asset insurance.

The NAIC began a number of initiatives over the past few years to address the additional risk that life insurers have taken on in their investment portfolios over the last decade to increase yield. Specifically, the NAIC finalized new disclosure requirements on the collateral backing the value of collateral loans as well as any overcollateralization. The NAIC also adopted a Question and Answer Implementation Guide related to the new Principles-Based Bond definition, which became effective at the beginning of the year. The Guide serves to address the accounting and reporting of fixed income instruments that may contain provisions preventing bond treatment under the new guidance. The NAIC also continued to make improvements to its requirements dealing with private credit and, more specifically, private letter ratings issued by credit rating providers. While such ratings have been required for some time, more stringent timing requirements were adopted along with more specific requirements with respect to the adequacy of the ratings rationale. Failure to meet either of these new requirements will lead to deactivation of the NAIC designation on the related security.

The NAIC also adopted new reporting requirements that detail the composition of life insurers assets by type and NAIC designation for modified coinsurance agreements and funds withheld agreements. Both types of agreements are used for life and annuity businesses in particular to limit credit risk that the ceding company has with the reinsurer by requiring collateral from the reinsurer. These agreements are typically more common in reinsurance with non-U.S. reinsurers, including those where collateral is required for regulatory purposes and also those where collateral is not required for regulatory purposes but used for commercial purposes.

Similarly, the NAIC also adopted new reporting requirements that restrict the use of assets involved in these same types of modified coinsurance or funds withheld agreements if they are already used for other purposes, such as collateral in FHLB transactions or repurchase

or securities lending agreements. The same disclosure was also expanded to provide transparency in cases where the reinsurer is investing on behalf of the cedent through an affiliate or related parties. These changes were introduced largely in response to the increased use of such agreements beginning in 2010 when many insurers sought to reinsurance their spread-based annuity business as a result of lower interest rates. The trend has continued and increased since 2021 as a result of the higher interest rates, which have led to a substantial increase in fixed annuity and indexed annuity business sold. Third-party capital interjected through sidecars or reinsurers in countries outside of the U.S., including most notably Bermuda, has contributed to these trends.

The NAIC and state regulators have responded to these risks through the NAIC's adoption of Actuarial Guideline 55. This actuarial guideline requires additional disclosures on reinsurance contracts that meet certain materiality requirements. Specifically, the actuarial guideline requires additional disclosures to ensure that adequate assets exist between the ceding and assuming entities to support the pre-reinsurance business. Depending on the risk of the reinsurance treaty, the actuarial guideline requires that the additional disclosures include cash flow testing, attribution analysis, or other analyses that illustrate the difference between the level of pre-reinsurance reserves compared to the retained and assumed level of reserves post-reinsurance. Similar actuarial reports used in other jurisdictions may be provided in place of the additional disclosures if they meet certain requirements.

## 5.3 Financial Infrastructure, Markets, and Oversight

### 5.3.1 Digital Assets, Payment Systems, and Technological Innovation

The SEC staff has clarified the security status of certain types of digital assets. On February 27, 2025, the SEC's Division of Corporation Finance expressed its view that meme coins—which are generally purchased for entertainment or other social or cultural purposes and whose value is driven by market demand and speculation—are akin to collectibles and generally are not securities. On April 4, 2025, the Division expressed

its view that certain U.S. dollar-based, non-yield-bearing stablecoins are not securities.

On March 7, 2025, the OCC issued OCC Interpretive Letter 1183, which reaffirmed that the crypto asset activities addressed in Interpretive Letters 1170, 1172, and 1174 remain permissible. The letter also rescinded OCC Interpretive Letter 1179 and eliminated the supervisory non-objection process detailed in that letter. On May 7, the OCC issued Interpretive Letter 1184, which provided further clarification regarding permissible crypto asset custody services.

Similarly, the SEC's Division of Corporation Finance has clarified the security status of certain blockchain-related activities. On March 20, 2025, the Division provided its view that proof-of-work mining activities generally do not constitute securities transactions. On May 29, 2025, the Division expressed its view that certain staking activities in connection with a proof-of-stake blockchain protocol are not securities transactions. On August 5, 2025, the Division expressed its view that liquid staking, a type of protocol staking activity, generally is not a securities transaction.

On March 28, 2025, the FDIC provided new guidance for FDIC-supervised institutions, affirming that these institutions may engage in permissible activities including those involving new and emerging technologies such as crypto assets and digital assets, provided they adequately manage the associate risks.

On April 10, 2025, the SEC's Division of Corporation Finance issued guidance on disclosure requirements as they apply to offerings and registrations of securities in the crypto asset markets. On May 15, 2025, the Division of Trading and Markets withdrew a joint staff statement with the Financial Industry Regulatory Authority (FINRA) that restricted broker-dealer activities with respect to digital assets that are securities. On the same day, the Division issued a set of frequently asked questions providing guidance regarding the application of certain regulatory requirements to registrants engaged in crypto assets activities or using DLT in their operations. On July 1, 2025, the Division of Corporation Finance provided its views on how certain disclosure requirements apply to offerings and

registrations of securities by issuers of crypto-related exchange-traded products.

On April 24, 2025, the Federal Reserve and FDIC joined the OCC in withdrawing two joint statements regarding banking organizations' crypto asset activities. Additionally, the Federal Reserve and FDIC withdrew supervisory letters establishing expectations that banks provide prior notification of planned or current digital asset activities, and the Federal Reserve and OCC withdrew letters regarding supervisory non-objection processes for bank engagement in dollar token activities and digital asset activities, respectively. These changes improve clarity that banking organizations may engage in permissible crypto asset activities and provide products and services to persons and firms engaged in crypto asset related activities consistent with safety and soundness and applicable laws and regulations.

On July 14, 2025, the Federal Reserve, FDIC, and OCC issued a joint statement that discusses existing risk management principles that apply to crypto asset safekeeping.

On August 15, 2025, the Federal Reserve announced that it would sunset its novel activities supervision program and return to monitoring banks' novel activities through the normal supervisory process.

In 2025, Colorado, Massachusetts, Mississippi, Nebraska, and Virginia signed into law legislation based on the Conference of State Bank Supervisors (CSBS) Money Transmission Modernization Act (MTMA), bringing the total number of fully enacted state MTMA laws to 27. The MTMA enhances prudential standards for money transmitters, including requirements related to tangible net worth, surety bonds, and the types and maintenance of permissible investments. At the end of the second quarter of 2024, companies subject to the MTMA facilitated 99 percent of money transmission activity reported through the Nationwide Multistate Licensing System Money Services Businesses Call Report, or \$5.359 billion of the total \$5.416 billion. Additionally, companies subject to the MTMA's capital and safeguarding requirements include but are not limited to the top 50 money services businesses.

The SEC staff has issued no-action letters in connection with certain crypto-asset related activities. On September 29, 2025, the Division of Corporation Finance issued a letter stating that it would not recommend enforcement action against a firm that has established a programmatic protocol with an accompanying token to facilitate a market in high-performance fiber network connectivity. On September 30, 2025, the Division of Investment Management issued a no-action letter stating that it would not recommend enforcement action against a registered investment adviser or against a regulated investment company for using a state trust company as a qualified custodian for crypto assets under certain conditions.

### **Rulemaking to Implement the Guiding and Establishing National Innovation for U.S. Stablecoins Act**

On September 19, 2025, Treasury issued an advance notice of proposed rulemaking (ANPR) to solicit public comment on questions relating to the implementation of the GENIUS Act. The GENIUS Act tasks Treasury (and various other federal agencies) with issuing regulations that encourage innovation in payment stablecoins while also providing an appropriately tailored regime to protect consumers, mitigate potential illicit finance risks, and address financial stability risks. Through this ANPR, Treasury sought public comment on potential regulations that may be promulgated by Treasury including on enhancing regulatory clarity, prohibitions on certain issuances and marketing, BSA / AML and sanctions obligations, the balance of state-level oversight with federal oversight, comparable foreign regulatory and supervisory regimes, and tax issues, among other things.

### **5.3.2 Derivatives, Swap Data Repositories, Regulated Trading Platforms, Central Counterparties, and Financial Market Utilities**

On January 22, 2025, the CFTC issued a final rule amending its regulations governing the types of investments that futures commission merchants and derivatives clearing organizations may make with funds held for the benefit of customers engaging in futures, foreign futures, and cleared swaps transactions. The CFTC also revised asset-based and issuer-based concentration limits for

the investment of customer funds. The CFTC also specified market risk capital charges that a futures commission merchant must take on new investments added to the list of permitted investments in computing the firm's adjusted net capital. The amendments also revise regulations that require each futures commission merchant to report to the CFTC and to the firm's designated self-regulatory organization, the name, location, and amount of customer funds held by each depository, including any investments of customer funds held by the depository.

On January 22, 2025, the CFTC also issued a final rule to implement requirements for futures commission merchants related to margin adequacy and the treatment of separate accounts of a customer.

On February 28, 2025, the SEC approved the registration of the first of eight security-based swap execution facilities (SBSEFs) under the Exchange Act.

On April 17, 2025, the SEC extended until November 5, 2029 the expiration date of a compliance statement related to Regulation SBSR, on reporting and dissemination of security-based swap transaction information, and security-based swap data repository rules that promotes harmonization with the CFTC's swap reporting and swap data repository rules.<sup>138</sup>

### **5.3.3 Securities and Asset Management**

On March 4, 2025, the SEC extended the compliance date for the amendments to the rules applicable to covered clearing agencies (CCAs) for U.S. Treasury securities (U.S. Treasury securities CCAs), which require that such CCAs have written policies and procedures reasonably designed to require that every direct participant of the CCA submit for clearance and settlement all eligible secondary market transactions in U.S. Treasury securities to which it is a counterparty and to identify and monitor its direct participants' submission of transactions for clearing, including how the U.S. Treasury securities CCA would address a failure to submit transactions that were adopted on December 13, 2023. Specifically, the SEC extended the compliance dates by one year from December 31, 2025, to December 31, 2026, for eligible cash market transactions and from June 30, 2026, to June 30, 2027, for eligible repo transactions.

On April 22, 2025, the SEC delayed the effective date for the amendments to Form N-PORT that were published on September 11, 2024, from November 17, 2025, to November 17, 2027. The SEC also delayed the effective date of the amendments to the rule under the Investment Company Act of 1940 associated with Form N-PORT reporting requirements. In addition, the SEC delayed the compliance dates for these amendments related to Form N-PORT reporting requirements. The effective and compliance date for the amendments to Form N-CEN contained in the same release published on September 11, 2024, will remain November 17, 2025.

On September 17, 2025, the SEC and CFTC extended the compliance date for the amendments to Form PF that were adopted on February 8, 2024, to October 1, 2026. The compliance date was previously extended to June 12, 2025, and then October 1, 2025. Form PF is the confidential reporting form for certain SEC-registered investment advisers to private funds including those also registered with the CFTC as a commodity pool operator or commodity trading adviser.

On September 17, 2025, the SEC issued a policy statement concluding that the mandatory use of arbitration to resolve disputes between a company and its shareholders is not inconsistent with the federal securities laws. Following this policy statement and subject to state corporate law, companies may choose to adopt mandatory arbitration provisions in their governing documents. To the extent companies adopt these provisions, they could decrease costs associated with frivolous litigation.

### **5.3.4 Accounting Standards**

On January 23, 2025, the SEC published Staff Accounting Bulletin (SAB) No. 122 to rescind SAB No. 121. SAB No. 121, which was published in 2022, expressed the staff view that certain entities safeguarding digital assets should record both a liability and a corresponding asset on their balance sheets at the fair value of the assets held even if such assets were never lent by the entities, which may have discouraged publicly traded banks from offering custody services for digital assets.

The GENIUS Act prohibits the SEC, FDIC, OCC, NCUA, and Federal Reserve from requiring any depository institution, national bank, Federal credit union, State credit union, or trust company (or any affiliate thereof) to treat custodied digital assets as liabilities of the entity. The GENIUS Act also states that payment stablecoins cannot be treated as cash or cash equivalents for accounting purposes unless issued by a permitted payment stablecoin issuer, as defined by the GENIUS Act.

### **5.3.5 Bank Secrecy Act/Anti-Money Laundering Regulatory Reform**

#### **The Corporate Transparency Act**

On March 26, 2025, Treasury's Financial Crimes Enforcement Network (FinCEN) published an interim final rule (IFR) to narrow the beneficial ownership information (BOI) reporting requirements under the Corporate Transparency Act (CTA). Under the IFR, any entity previously defined as a "domestic reporting company" is no longer included in the regulatory definition of a "reporting company." The IFR exempts domestic entities from any BOI reporting requirements, and, therefore, these entities do not have to report BOI to FinCEN or update or correct BOI previously reported to FinCEN.

With limited exceptions, the IFR does not change the existing requirement for any entity previously considered a foreign reporting company to file BOI reports. The IFR did extend the deadline for these entities to file initial BOI reports and to update or correct previously filed BOI reports to 30 days from the IFR's publication date to give foreign reporting companies additional time to comply. The IFR also exempts foreign reporting companies from having to report the BOI of any U.S. person who is a beneficial owner of the reporting company. In addition, the IFR exempts any U.S. person from having to provide such information to any foreign reporting company for which they are a beneficial owner.

#### **Request for Comment Related to Innovative Methods to Detect Illicit Activity Involving Digital Assets**

On August 18, 2025, Treasury issued a request for comment required by the GENIUS Act, supporting the responsible growth and use of digital assets as outlined in EO 14178. This request offered

the opportunity for interested individuals and organizations to provide feedback on innovative or novel methods, techniques, or strategies that regulated financial institutions use or could potentially use to detect illicit activity involving digital assets.

In particular, Treasury asked commenters about application program interfaces, AI, digital identity verification, and the use of blockchain technology and monitoring. Innovative tools are critical to advancing efforts to address illicit finance risks but can also present new resource burdens for financial institutions. As required by the GENIUS Act, Treasury is using public comments to inform research on the effectiveness, costs, privacy and cybersecurity risks, and other considerations related to these tools and a report and recommendations to Congress.

#### **Exemptive Relief Order and Notice of Proposed Rulemaking to Delay the Effective Date of the Final Rule of the Investment Adviser Anti-Money Laundering / Countering the Financing of Terrorism Program and Suspicious Activity Reporting Rule**

Consistent with the Administration's regulatory reform agenda, on July 21, 2025, Treasury announced FinCEN's intention to delay the AML/CFT Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers and Exempt Reporting Advisers (IA AML Rule) to ensure appropriate consideration of the rule's costs and benefits. On August 5, 2025, FinCEN issued an order granting exemptive relief to certain investment advisers from complying with the requirements established in the final IA AML Rule. The IA AML Rule is set to become effective January 1, 2026, and the order exempted covered investment advisers from all requirements of the IA AML Rule until January 1, 2028. On September 19, 2025, FinCEN issued a notice of proposed rulemaking to extend the effective date of the IA AML Rule from January 1, 2026, until January 1, 2028.

#### **Exemption Order Related to Taxpayer Identification Number Collection and Customer Identification Program Requirements**

With the concurrence of and in coordination with FinCEN, on June 27, 2025, the FDIC, OCC, and NCUA, and on July 31, 2025, the Federal Reserve,

issued an exemption order to the Customer Identification Program (CIP) Rule permitting a bank to obtain Taxpayer Identification Number (TIN) information (e.g., an individual's social security number) from a third party rather than directly from a bank's customer. Among other requirements, a bank is required under the CIP Rule to establish and implement written procedures that: (1) enable the bank to obtain TIN information prior to opening an account; (2) are based on the bank's assessment of the relevant risks; and (3) are risk based for the purpose of verifying the identity of each customer to the extent reasonable and practicable, enabling the bank to form a reasonable belief that it knows the true identity of each customer.

Under this exemption order, a bank is neither expected nor required to use an alternative collection method to obtain TIN information. FinCEN and the agencies considered the significant innovation in identity verification tools available to banks, among other factors, in granting this exemption.

### The Financial Action Task Force

The Financial Action Task Force (FATF) is the intergovernmental body that sets standards and promotes effective implementation of legal, regulatory, and operational measures for combating money laundering, terrorist financing, the financing of proliferation, and other related threats to the integrity of the international financial system. In collaboration with other international stakeholders, the FATF also works to identify national-level vulnerabilities to protect the international financial system from misuse.

In February 2024, the FATF agreed to upgrade the United States from “noncompliant” to “largely compliant” with the FATF Recommendation 24, which relates to transparency and beneficial ownership of legal persons. Following this decision, in March 2024, FATF published the updated rating in the Seventh Enhanced Follow-Up Report of the United States. Recommendation 24 is currently being reassessed as part of the next FATF 2026 Mutual Evaluation of the United States.

In October 2024, the FATF adopted new guidance for governments on how to assess risks related to money laundering. In June 2025, FATF adopted and published two reports on terrorist financing,

proliferation financing, and sanctions evasion that will inform how the public and private sectors assess and mitigate illicit finance risk in the financial system. First, FATF endorsed its first update for major global terrorist financing trends and risks in a decade, which will help the public and private sectors better understand the nature of global risks, trends, and methodologies related to the financing of terrorism. Second, the task force endorsed a new report on proliferation financing and sanctions evasion, following the dissolution of the United Nations 1718 Panel of Experts last year. The report culminated with 40 case studies and typologies about how illicit actors associated with Iran, North Korea, and Russia evade sanctions and highlights how North Korea raises revenue for its weapons of mass destruction program.

In 2024, the FATF published two reports on virtual assets. The first highlights progress in implementation of the FATF standards for virtual assets, and the second outlines good practices for supervising Recommendation 16 in virtual assets. The FATF will continue to promote implementation of the FATF standards for virtual assets by all countries, discuss emerging threats in the virtual asset ecosystem, and develop resources through targeted projects to support effective implementation.

In June 2025, the FATF adopted revisions to the FATF Recommendation on payment transparency (Recommendation 16). These revisions were necessary to account for changes in the payments landscape, ensure the standard remains technology neutral, and reflect changes to industry standards, in particular, ISO 20022. Over the next year, the FATF will produce a guidance document to help facilitate implementation and will update its methodology to reflect the revisions. The updated Recommendation 16 will not be fully in force until 2030.

On October 9, 2025, the OCC, Federal Reserve, FDIC, NCUA, and FinCEN clarified regulatory requirements related to Suspicious Activity Reports (SARs) by issuing answers to frequently asked questions. These answers clarify regulatory requirements related to SARs and can assist financial institutions with their compliance obligations, while enabling institutions to focus resources on activities that produce the greatest value to law enforcement agencies and other government users of BSA reporting.

## **5.4 Mortgages and Housing Finance**

On July 28, 2025, the FHFA requested comment on a notice of proposed rulemaking repealing the Fair Lending, Fair Housing, and Equitable Housing Finance Plans regulation.

On October 2, 2025, the FHFA issued a proposed rule and requested comments on the housing goals for Fannie Mae and Freddie Mac for 2026 through 2028 as required by the Federal Housing Enterprises Financial Safety and Soundness Act of 1992. The proposed rule establishes benchmark levels for the housing goals for 2026 through 2028. The proposed rule replaces the two area-based subgoals with one low-income areas subgoal, simplifies the goal determination process, clarifies inflation adjustments to maximum civil money penalties related to housing goals, and makes other technical changes.

On October 6, 2025, the OCC issued a notice of proposed rulemaking to rescind a regulation that required national banks to collect and retain certain information on applications for home loans.

During 2025, Arkansas, Georgia, Nevada, North Carolina, and Wisconsin enacted legislation based on the CSBS Model State Regulatory Prudential Standards for Nonbank Mortgage Servicers, resulting in a total of 12 states adopting the prudential standards. These standards require nonbank mortgage servicers to maintain the financial capacity, corporate governance, and risk management practices sufficient to adequately serve consumers and investors and simultaneously enhance market stability. Given the multistate operations of most nonbank mortgage firms, the states that have adopted the prudential standards effectively cover 99 percent of the nonbank mortgage market by loan count, including, but not limited to, the 50 largest nonbank mortgage servicers.

# Section 6. Abbreviations

<b>AI</b>	Artificial Intelligence
<b>AML</b>	Anti-Money Laundering
<b>AML Act</b>	Anti-Money Laundering Act of 2020
<b>AML/CFT</b>	Anti-Money Laundering/Countering the Financing of Terrorism
<b>ANPR</b>	Advance Notice of Proposed Rulemaking
<b>AUM</b>	Assets Under Management
<b>BDC</b>	Business Development Company
<b>BOI</b>	Beneficial Ownership Information
<b>BSA</b>	Bank Secrecy Act
<b>CAIO</b>	Chief Artificial Intelligence Officer
<b>CCP</b>	Central Counterparty
<b>CET1</b>	Common Equity Tier 1 Capital
<b>CFPB</b>	Consumer Financial Protection Bureau
<b>CFT</b>	Countering the Financing of Terrorism
<b>CFTC</b>	Commodity Futures Trading Commission
<b>CIF</b>	Collective Investment Fund
<b>CIP Rule</b>	Customer Identification Program Rule
<b>CLO</b>	Collateralized Loan Obligation
<b>CMBS</b>	Commercial Mortgage-Backed Security
<b>CME</b>	Chicago Mercantile Exchange Inc.
<b>CNAV</b>	Constant Net Asset Value
<b>Council</b>	Financial Stability Oversight Council
<b>CRE</b>	Commercial Real Estate
<b>CSBS</b>	Conference of State Bank Supervisors
<b>CTA</b>	Corporate Transparency Act
<b>DDoS</b>	Distributed Denial of Service
<b>Dodd-Frank Act</b>	Dodd-Frank Wall Street Reform and Consumer Protection Act
<b>Digital Asset Report</b>	July 2025 report by the President's Working Group on Digital Asset Markets
<b>DPRK</b>	Democratic People's Republic of Korea
<b>DLT</b>	Distributed Ledger Technology
<b>DTCC</b>	Depository Trust & Clearing Corporation
<b>DvP</b>	Delivery-versus-Payment

<b>eSLR</b>	Enhanced Supplementary Leverage Ratio
<b>ETF</b>	Exchange-Traded Fund
<b>EO</b>	Executive Order
<b>FABN</b>	Funding Agreement Backed Note
<b>Fannie Mae</b>	Federal National Mortgage Association
<b>FBIIC</b>	Financial and Banking Information Infrastructure Committee
<b>FDIC</b>	Federal Deposit Insurance Corporation
<b>FHA</b>	Federal Housing Administration
<b>FHFA</b>	Federal Housing Finance Agency
<b>FHLB</b>	Federal Home Loan Bank
<b>FICC</b>	Fixed Income Clearing Corporation
<b>FinCEN</b>	Financial Crimes Enforcement Network
<b>Fintech</b>	Financial Technology
<b>FIO</b>	Federal Insurance Office
<b>FOMC</b>	Federal Open Market Committee
<b>FRBNY</b>	Federal Reserve Bank of New York
<b>FRED</b>	Federal Reserve Economic Data
<b>Freddie Mac</b>	Federal Home Loan Mortgage Corporation
<b>GAV</b>	Gross Asset Value
<b>GDP</b>	Gross Domestic Product
<b>GenAI</b>	Generative Artificial Intelligence
<b>GENIUS Act</b>	Guiding and Establishing National Innovation for U.S. Stablecoins Act
<b>GFC</b>	Global Financial Crisis
<b>Ginnie Mae</b>	Government National Mortgage Association
<b>GSD</b>	Government Securities Division
<b>GSE</b>	Government-Sponsored Enterprise
<b>G-SIB</b>	Global Systemically Important Bank
<b>HPI</b>	FHFA House Price Index
<b>HQLA</b>	High-quality Liquid Assets
<b>IA AML Rule</b>	Anti-Money Laundering/Countering the Financing of Terrorism Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers and Exempt Reporting Advisers
<b>IAWG</b>	Inter-Agency Working Group for Treasury Market Surveillance
<b>ICE</b>	Intercontinental Exchange
<b>IDI</b>	Insured Depository Institution

<b>IFR</b>	Interim Final Rule
<b>IOSCO</b>	International Organization of Securities Commissions
<b>IT</b>	Information Technology
<b>LFI</b>	Large Financial Institution
<b>LGIP</b>	Local Government Investment Pool
<b>LLM</b>	Large Language Model
<b>LVNAV</b>	Low Volatility Net Asset Value
<b>MBS</b>	Mortgage-Backed Security
<b>MBSD</b>	Mortgage-Backed Securities Division
<b>MMF</b>	Money Market Fund
<b>MTMA</b>	Money Transmission Modernization Act
<b>NAIC</b>	National Association of Insurance Commissioners
<b>NAV</b>	Net Asset Value
<b>NBFI</b>	Nonbank Financial Institution
<b>NCCBR</b>	Non-centrally Cleared Bilateral Repo
<b>NCD</b>	Negotiable Certificate of Deposit
<b>NCUA</b>	National Credit Union Administration
<b>NDFI</b>	Non-Depository Financial Institution
<b>NDLs</b>	Non-Default Losses
<b>NBER</b>	National Bureau of Economic Research
<b>NIM</b>	Net Interest Margin
<b>NOI</b>	Net Operating Income
<b>NPL</b>	Nonperforming Loan
<b>NSCC</b>	National Securities Clearing Corporation
<b>OCC</b>	Office of the Comptroller of the Currency
<b>OEF</b>	Open-End Fund
<b>OFR</b>	Office of Financial Research
<b>ON RRP</b>	Overnight Reverse Repo Facility
<b>OTC</b>	Over-the-Counter
<b>P&amp;C</b>	Property and Casualty
<b>PE</b>	Private Equity
<b>PIK</b>	Payment-in-Kind
<b>PRC</b>	People's Republic of China
<b>Repo</b>	Repurchase Agreement
<b>RRE</b>	Residential Real Estate

<b>S&amp;P</b>	Standard and Poor's
<b>SEC</b>	Securities and Exchange Commission
<b>SLOOS</b>	Senior Loan Officer Opinion Survey
<b>SOFR</b>	Secured Overnight Financing Rate
<b>SRC</b>	Systemic Risk Committee
<b>SRF</b>	Federal Reserve's Standing Repo Facility
<b>STIF</b>	Short-Term Investment Fund
<b>STIV</b>	Short-Term Investment Vehicle
<b>TGCR</b>	Tri-Party General Collateral Rate
<b>TIN</b>	Taxpayer Identification Number
<b>Treasury</b>	U.S. Department of the Treasury
<b>TRIP</b>	Terrorism Risk Insurance Program
<b>TTX</b>	Tabletop Exercise
<b>VNAV</b>	Variable Net Asset Value

# Section 7. Glossary

## Artificial Intelligence

As stated in EO 14179 referencing 15 U.S.C. 9401(3), artificial intelligence is a machine-based system that can, for a given set of human-defined objectives, make predictions, recommendations, or decisions influencing real or virtual environments.

## Assets Under Management (AUM)

The total market value of investments that an entity manages on behalf of clients.

## Bilateral Repo

A repo between two institutions in which the participants conduct negotiations directly between them or through a broker and the participants agree on the specific securities to be used as collateral. The bilateral repo market includes both noncleared trades and trades cleared through Fixed Income Clearing Corporation's delivery versus payment (DVP) repo service.

## Blockchain

EO No. 14178 defines a blockchain as "any technology where data is: (i) shared across a network to create a public ledger of verified transactions or information among network participants; (ii) linked using cryptography to maintain the integrity of the public ledger and to execute other functions; (iii) distributed among network participants in an automated fashion to concurrently update network participants on the state of the public ledger and any other functions; and (iv) composed of source code that is publicly available." Blockchain is often used interchangeably with DLT, but they are distinct and different technologies.

## Business Development Company

A form of closed-end investment company in the United States that invests in small and mid-sized businesses and that elects to be regulated under certain provisions of the Investment Company Act of 1940.

## Call Reports

Also known as Consolidated Reports of Condition and Income, these quarterly regulatory filings

are submitted by banks to the Federal Financial Institutions Examination Council (FFIEC), detailing their financial condition and result of operations.

## Cash-Futures Basis Trade

A trade where hedge funds arbitrage price inefficiencies between cash Treasury and future markets. Generally, the trade involves funds taking long positions in cash Treasuries while shorting corresponding futures contracts. The spreads between futures and underlying Treasuries, or basis, are small so hedge funds must deploy leverage to amplify returns. Leverage is usually obtained through repo borrowing against underlying Treasuries.

## Central Counterparty (CCP)

An entity that interposes itself between counterparties to trade in one or more financial markets, becoming the buyer to every seller and the seller to every buyer, thereby ensuring the performance of open contracts.

## Collateral

Any asset pledged by a borrower to guarantee payment of a debt.

## Collateralized Loan Obligation (CLO)

A securitization vehicle backed predominantly by commercial loans.

## Collective Investment Fund (CIF)

A bank-managed fiduciary fund that holds pooled assets; the bank is required to establish and operate the CIF in accordance with specific criteria established by the OCC.

## Commercial Mortgage-Backed Securities (CMBS)

Fixed-income investment products that are backed by mortgages on commercial properties rather than residential real estate.

## Commercial Paper

Short-term (maturity of up to 270 days), unsecured corporate debt.

## **Common Equity Tier 1 (CET1) Capital**

A regulatory capital measure that includes capital with the highest loss-absorbing capacity, such as common stock and retained earnings.

## **Common Equity Tier 1 Capital Ratio**

A ratio that divides CET1 capital by total risk-weighted assets. The ratio applies to all banking organizations subject to the Revised Capital Rule.

## **Community Banks**

Banks with less than \$10 billion in assets.

## **Crypto Asset**

Generally refers to any digital asset implemented using cryptographic techniques

## **Designated Financial Market Utility**

A financial market utility that has been designated by the Council under 12 CFR Part 1320 per the Council's determination that the financial market utility is, or is likely to become, systemically important (meaning, the financial market utility's failure or disruption could threaten the stability of the U.S. financial system). See *financial market utility*.

## **Digital Assets**

As noted in EO Number 14178, any digital representation of value that is recorded on a distributed ledger, including cryptocurrencies, digital tokens, and stablecoins.

## **Distributed Denial of Service (DDoS)**

A type of cyber attack where attackers disrupt operations by overwhelming targeted systems with malicious traffic and can disable firms' abilities to communicate with customers, undermining consumer confidence.

## **Distributed Ledger Technology (DLT)**

The protocols and supporting infrastructure that allow computers in different locations to propose and validate transactions and update records in a synchronized way across a network. See also *blockchain*.

## **Enhanced Supplementary Leverage Ratio (eSLR)**

A measure of a bank's tier 1 capital relative to its total leverage exposure; applies to U.S. bank holding companies identified as G-SIBs and their depository institution subsidiaries.

## **Federal Funds Rate**

The interest rate at which depository institutions borrow overnight from lenders in the federal funds market. The FOMC sets a target range for the level of the overnight federal funds rate. The FRBNY then uses open-market operations to influence the rate so that it trades within the target range.

## **Financial and Banking Information Infrastructure Committee (FBIIC)**

A committee composed of 18 member organizations from across the financial regulatory community, both federal and state. FBIIC was chartered under the President's Working Group on Financial Markets following September 11, 2001, to improve coordination and communication among financial regulators, enhance the resilience of the financial sector, and promote public-private partnerships.

## **Financial Market Utility**

A financial market utility as defined in the Dodd-Frank Act, an entity that, subject to certain exclusions, "manages or operates a multilateral system for the purpose of transferring, clearing, or settling payments, securities, or other financial transactions among financial institutions or between financial institutions and the person.

## **FMU Committee**

The Council's Financial Market Utilities and Payment, Clearing, and Settlement Activities (FMU) Committee.

## **Futures Contract**

An agreement to purchase or sell a commodity for delivery in the future that (1) specifies a buy or sell price determined at the initiation of the contract, (2) obligates each party to the contract to fulfill the contract at the specified price, (3) is used to assume or shift price risk, and (4) may be satisfied by delivery or offset.

## **Funding Agreement Backed Notes**

Securities that are backed by a funding agreement, which is a deposit-type contract, issued by life insurance companies, that promises a stream of predictable fixed payments over a specified period.

## **Global Systemically Important Bank (G-SIB)**

A bank with over \$250 billion in assets that regulators have identified as being so important to the global financial system that its failure could trigger a wider financial crisis.

## **Gross Asset Value**

The market value of balance sheet assets.

## **High-Yield Bond**

High-yield bonds that typically pay higher interest rates than investment grade bonds because the companies that issue them have lower credit ratings.

## **Initial Margin**

Collateral that is collected to cover potential changes in the value of each participant's position (that is, potential future exposure) over the appropriate closeout period in the event the participant defaults.

## **Interest Rate Swap (IRS)**

A derivative contract in which two parties swap interest rate cash flows on a periodic basis, referencing a specified notional amount for a fixed term. Typically, one party will pay a predetermined fixed rate while the other party will pay a short-term variable reference rate that resets at specified intervals.

## **Large Language Model (LLM)**

A subset of machine learning that uses algorithms trained on large amounts of data to recognize patterns and respond to user requests in natural language.

## **Leveraged Loan**

Generally, a type of loan that is extended to companies that already have considerable amounts of debt, have a noninvestment-grade credit rating, are unrated, or have post-financing leverage that significantly exceeds industry norms or historical levels. Numerous other definitions of leveraged lending exist throughout the financial services industry.

## **Local Government Investment Pools (LGIP)**

Typically, joining together the resources of participating governments and to be able to invest in various securities as permitted under state law. By pooling their cash together, participating

governments may benefit in a variety of ways, including from economies of scale and fund management.

## **Margin**

In the context of clearing activity, collateral that is collected to protect against current or potential future exposures resulting from market price changes or in the event of a counterparty default.

## **Modified Coinsurance**

A type of reinsurance treaty wherein the ceding company retains the assets with respect to policies reinsured and also establishes and maintains reserves on those policies, creating the obligation to render payments to the reinsurer at a later date.

## **Money Market Fund (MMF)**

A type of mutual fund that invests in short-term, high-quality, liquid securities such as government bills, CDs, commercial paper, or repos.

## **Mortgage-Backed Security (MBS)**

An asset-backed security backed by a pool of mortgages. Investors in the security receive payments derived from the interest and principal payments on the underlying mortgages.

## **Municipal Bonds**

Bonds issued by states, cities, counties, or local governmental agencies, including bonds issued on behalf of certain nongovernmental entities, to finance certain general or project-related activities.

## **Negotiable Certificates of Deposit (NCD)**

A bank-issued money-market instrument that can be traded between parties through money brokers.

## **Net Asset Value (NAV)**

An investment company's total assets minus its total liabilities.

## **Net Interest Margin (NIM)**

Net interest income as a percent of interest-earning assets.

## **Net Operating Income (NOI)**

A metric that measures the profitability of an investment or asset by subtracting operating expenses from income. It is often used in commercial real estate to evaluate the profitability of properties.

**Nonbank Financial Institution (NIFI) or Non-depository Financial Institution (NDFI)**  
A financial institution that does not have a full banking license and cannot accept deposits from the public. Examples of NBFIs/NDFIs include insurance firms, investment funds, venture capitalists, currency exchanges, and some microloan organizations, among others. These NBFIs/NDFIs provide services that are not necessarily suited to banks, serve as competition to banks, and specialize in sectors or groups.

**Nonbank Mortgage Company (NBMC)**  
A financial institution that offers mortgage lending services but is not a traditional bank. NBMCs offer a variety of services, including first-time home loans, refinancing, and more. NBMCs are not subject to the same regulations as traditional banks.

### **Non-Centrally Cleared Bilateral Repo (NCCBR)**

A transaction between two parties that involves the sale of securities in exchange for cash with an agreement to repurchase the securities at a later date.

### **Non-Default Loss (NDL)**

A loss that occurs at a central counterparty (CCP) as a result of an event other than a clearing member defaulting. NDLs can include losses from: cash and securities collateral provided to the CCP by its members, the CCP's own resources, operational risks, custody risks, and investment risks.

### **Non-Performing Loan (NPL)**

A bank loan that is unlikely to be repaid by the borrower or is subject to late repayment.

### **Off-Balance Sheet Leverage**

Also known as “synthetic leverage,” this refers to using instruments (such as derivatives) to create exposures whose value depends on an underlying asset.

### **Offshore MMFs**

Similar to U.S. MMFs but domiciled outside the United States, the offshore MMFs considered in this report invest in assets denominated in U.S. dollars.

### **Offshore Reinsurance**

A reinsurance arrangement between an insurance company and a reinsurer that is not licensed in the United States.

### **Over-the-Counter (OTC)**

A method of trading that does not involve a registered exchange. An OTC trade could occur on purely a bilateral basis or could involve some degree of intermediation by a platform that is not required to register as an exchange.

### **Overnight Reverse Repurchase Agreement Facility (ON RRP)**

Overnight reverse repo transactions conducted by the Federal Reserve Bank of New York to support the effective implementation of monetary policy and smooth market functioning. Provides a floor under overnight interest rates by acting as an alternative investment for a broad base of money market investors.

### **Payment-in-Kind (PIK)**

A loan feature that allows borrowers to defer interest payments, and, instead, add them onto the principal of the loan.

### **Payment Stablecoin**

A digital asset issued for payment or settlement and redeemable at a predetermined fixed amount.

### **Primary Dealer**

A financial institution that is a trading counterparty of the FRBNY. Primary dealers are expected to participate in open-market operations conducted by the Federal Reserve and to bid on a pro rata basis in all Treasury auctions at reasonably competitive prices.

### **Private Liquidity Funds**

Structurally similar to MMFs, but only open to certain qualified investors, these funds often serve as the investment vehicle for large pools of cash collateral generated by securities lending activity.

### **Qualifying Hedge Fund**

A hedge fund that is advised by a Large Hedge Fund Adviser and that has a NAV (individually or in combination with any feeder funds, parallel funds, or dependent parallel managed accounts) of at least \$500 million as of the last day of any month in the fiscal quarter immediately preceding the adviser’s most recently completed fiscal quarter.

### **Regional Banks**

Banks with assets between \$10 billion and \$250 billion.

## **Repurchase Agreement (Repo)**

The sale of a security combined with an agreement to repurchase the security, or a similar security, on a specified future date at a prearranged price. A repo is a secured lending arrangement.

## **Risk-Weighted Assets (RWAs)**

A risk-based concept used as the denominator of risk-based capital ratios (common equity Tier 1, Tier 1, and total). The total RWAs for an institution are a weighted total asset value calculated from assigned risk categories or modeled analysis. Broadly, total RWAs are determined by calculating RWAs for market risk and operational risk, as applicable, and adding the sum of RWAs for on-balance sheet, off-balance sheet, counterparty, and other credit risks.

## **Secured Overnight Financing Rate (SOFR)**

A broad measure of the cost of borrowing cash overnight, collateralized by Treasury securities. The rate is calculated as a volume-weighted median of transaction-level tri-party repo data, as well as general collateralized financing repo transaction data and data on bilateral Treasury repo transactions.

## **Securities Lending and Borrowing**

The temporary transfer of securities from one party to another for a specified fee and term in exchange for collateral in the form of cash or securities.

## **Short-Term Investment Fund (STIF)**

A type of CIF, investment vehicles sponsored by banks or trusts that pool assets for eligible clients with whom the bank has a fiduciary relationship. STIF investments are limited to shorter-term assets and typically operate with the primary objective of maintaining a stable net asset value.

## **Short-Term Investment Vehicle (STIV)**

An asset that can be converted to cash or sold within a short period. Short-term investments are often used to meet financial goals in the near future. Types of STIVs include local government investment pools (LGIPs), dollar-denominated MMFs domiciled outside of the U.S. (offshore U.S. Dollar MMFs), private liquidity funds, bank-sponsored short-term investment funds (STIFs), and ultrashort bond funds.

## **Short-Term Wholesale Funding**

Short-term funding instruments that are not covered by deposit insurance and that are typically issued to institutional investors. Examples include large checkable and time deposits, brokered CDs, commercial paper, Federal Home Loan Bank borrowings, and repos.

## **Standing Repo Facility (SRF)**

Overnight repo transactions conducted by the Federal Reserve Bank of New York to support the effective implementation of monetary policy and smooth market functioning. The SRF serves as a backstop to dampen upward interest rate pressures that can occasionally emerge in overnight U.S. dollar funding markets and spillover into the federal funds market.

## **Supplementary Leverage Ratio (SLR)**

Measures a bank's tier 1 capital relative to its total leverage exposure.

## **Swap**

An exchange of cash flows with defined terms over a fixed period agreed upon by two parties. A swap contract may reference underlying financial products across various asset classes, including interest rates, credit, equities, commodities, and foreign exchange.

## **Ultrashort Bond Funds**

Mutual funds that generally invest in fixed-income securities with extremely short maturities (that is, time periods in which they become due for payment). Like other bond funds, ultrashort bond funds may invest in a wide range of securities.

## **VantageScore**

A tri-bureau credit scoring model that assigns consumers a credit score between 300 and 850 based on their credit history.

## **Variation Margin**

Funds that are collected and paid out to reflect current exposures resulting from actual changes in market.

# Section 8. List of Charts

3.1.1 U.S. Marketable Debt Held by the Public .....	12
3.1.2 Total TRACE U.S. Treasury Daily Volume.....	13
3.1.3 U.S. Treasury Market Liquidity Indexes.....	13
3.1.4 Holders of Treasury Securities .....	14
4.1.1.1 Commercial Paper Outstanding by Issuer Type.....	26
4.1.1.2 One-Month Commercial Paper Interest Rate Spreads.....	26
4.1.1.3 Repo Transaction Volumes.....	27
4.1.1.4 Overnight Repo Spreads .....	27
4.1.1.5 MMF Total Net Assets by Type .....	28
4.1.2.1 Year-Over-Year Change in Net Operating Income by Property Type.....	30
4.1.2.2 Vacancy Rates by Property Type.....	30
4.1.2.3 Bank CRE Delinquency Rates by Asset Size .....	31
4.1.2.4 Bank CRE Concentrations by Asset Size.....	31
4.1.3.1 Corporate Bond and Leveraged Loan Yields.....	32
4.1.3.2 Corporate Bond and Leveraged Loan Spreads .....	32
4.1.3.3 Year-to-Date Gross Issuance.....	32
4.1.3.4 Interest Coverage Ratios .....	33
4.1.3.5 Par-Weighted Default Rates .....	33
4.1.3.6 Bankruptcy Filings.....	33
4.1.3.7 Private Credit Fund AUM.....	34
4.1.4.1 Household Debt to GDP by Major Categories.....	36
4.1.4.2 Debt Service to Disposable Personal Income by Category.....	36
4.1.4.3 Share of Balances 30+ Days Delinquent by Loan Type .....	36
4.1.4.4 Average Credit Score Among Student Loan Borrowers by New Delinquency Status.....	37
4.1.4.5 Projected Months of Covered Expenses for Households .....	37
4.1.5.1 House Price Index .....	38
4.1.5.2 30-Year Fixed Rate Mortgage Interest Rate.....	38
4.1.5.3 Average Monthly Mortgage Payment.....	39
4.1.5.4 Quarterly Mortgage Originations .....	39
4.1.5.5 Outstanding Mortgages by Interest Rate .....	40
4.2.1.1 Return on Assets .....	44
4.2.1.2 Common Equity Tier 1 Ratios .....	44
4.2.1.3 Delinquency Rates on Selected Loans.....	45
4.2.1.4 Total Funding Rate, Yield on Earning Assets, and NIM .....	45
4.2.1.5 Income Composition (2024) .....	45

4.2.1.6 Loan Distribution by Bank Group.....	46
4.2.2.1 Hedge Fund Size.....	48
4.2.2.2 Hedge Fund Leverage by Size Cohort.....	48
4.2.2.3 Hedge Fund Leverage by Strategy.....	48
4.2.2.4 Unencumbered Cash Ratios of 10 Largest Funds.....	49
4.2.2.5 Hedge Fund Treasury Exposure.....	49
4.2.2.6 Mutual Fund AUM.....	50
4.2.2.7 Mutual Fund Net Flows.....	50
4.2.2.8 ETF AUM.....	50
4.2.2.9 ETF Net Flows .....	51
4.2.2.10 Collective Investment Fund AUM by Sector.....	51
4.2.3.1 DTCC Clearing Fund Requirements.....	53
4.2.3.2 Initial Margin: U.S. Exchange-Traded Derivatives.....	53
4.2.3.3 Initial Margin: Centrally Cleared OTC Derivatives.....	53
4.2.3.4 Average Time of U.S. CCP Operational Disruptions.....	53
4.2.4.1 Life Insurers' Changing Investment Portfolios.....	55
4.2.4.2 More Life Insurance Reserves Are Moving Offshore .....	56

# Section 9. Endnotes

- 1 Homeland Security Act of 2002, 6 U.S.C. § 474(c)(2)
- 2 The White House. (2025, July). *America's AI Action Plan*. <https://www.whitehouse.gov/wp-content/uploads/2025/07/Americas-AI-Action-Plan.pdf>
- 3 As of September 30, 2025, the total U.S. Treasury debt was approximately \$38 trillion with around 80 percent (over \$29 trillion) held by the public. \$29 trillion is the most economically meaningful figure, because it represents what is transacted in the credit markets and can influence interest rates.
- 4 In the “dash-for-cash” episode, investors broadly sold Treasury securities (and other global sovereign bonds) to meet redemptions, margin calls, and build cash buffers.
- 5 Other capital and liquidity regulations – including Basel III risk-based capital standards, requirements associated with large bank stress testing, and the Liquidity Coverage Ratio – can also influence bank demand for U.S. Treasuries.
- 6 In a June 2025 speech, Federal Reserve Vice Chair for Supervision Michelle W. Bowman noted that the increasing bindingness of the eSLR is an unintended consequence of market and other bank regulatory requirements implemented after the eSLR was put into place. Specifically, the original calibration of the eSLR was based on forecasted levels of reserves and other “safe assets” that are now considerably out of line with current levels. Bowman, M. W. (2025, June 6). *Taking a Fresh Look at Supervision and Regulation*. Federal Reserve. <https://www.federalreserve.gov/newsevents/speech/bowman20250606a.htm>
- 7 OCC, Federal Reserve, FDIC. (2025, December 1). *Regulatory Capital Rule: Modifications to the Enhanced Supplementary Leverage Ratio Standards for U.S. Global Systemically Important Bank Holding Companies and Their Subsidiary Depository Institutions; Total Loss-Absorbing Capacity and Long-Term Debt Requirements for U.S. Global Systemically Important Bank Holding Companies*. Federal Register. <https://www.govinfo.gov/content/pkg/FR-2025-12-01/pdf/2025-21626.pdf>
- 8 The cash-futures basis trade seeks to arbitrage small price differences between cash Treasury securities and related Treasury futures. Strong demand from asset managers for Treasury futures creates an opportunity to “go long the basis” by buying cash Treasury securities using repo financing and selling Treasury futures. Significant leverage is typically used to amplify profits. The trade may need to be abruptly unwound if repo financing becomes unstable or in the event of margin calls, triggering significant sales of cash Treasury securities.
- 9 The “on-the-run” Treasury security is the most recently issued Treasury security, and the “off-the-run” Treasury securities are all Treasury securities issued before the most recently issued Treasury security.
- 10 The bid-to-cover ratio equals the amount of offers at auctions divided by the offering amount. Stop-out rates are the rates awarded to auction participants.
- 11 CFTC. (2025, September). *Commitments of Traders*. <https://www.cftc.gov/MarketReports/CommitmentsofTraders/index.htm>
- 12 Treasury. (2024, May 1). *Quarterly Refunding Statement of Assistant Secretary of Financial Markets Josh Frost* [Press release]. <https://home.treasury.gov/news/press-releases/jy2315>
- 13 Federal Reserve. (2021, July 28). *Standing Repurchase Agreement Facility*. <https://www.federalreserve.gov/monetarypolicy/standing-overnight-repurchase-agreement-facility.htm>
- 14 OFR. (2024, May 6). *OFR Adopts Final Rule for Data Collection of Non-centrally Cleared Bilateral Transactions in the U.S. Repurchase Agreement Market* [Press release]. <https://www.financialresearch.gov/press-releases/2024/05/06/ofr-adopts-final-rule-for-data-collection>
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- 16 SEC. (2025, March). *Extension of Compliance Dates for Standards for Covered Clearing Agencies for U.S. Treasury Securities and Application of the Broker-Dealer Customer Protection Rule with Respect to U.S. Treasury Securities*. Release No. 34-102487; File No. S7-23-22 (17 CFR Part 240). <https://www.sec.gov/files/rules/final/2025/34-102487.pdf>
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- 18 The White House. (2025, June 6). *Sustaining Select Efforts to Strengthen the Nation's Cybersecurity and Amending Executive Order 13694 and Executive Order 14144*. <https://www.whitehouse.gov/presidential-actions/2025/06/sustaining-select-efforts-to-strengthen-the-nations-cybersecurity-and-amending-executive-order-13694-and-executive-order-14144/>; Federal Reserve. (2025, April). *Financial Stability Report*. <https://www.federalreserve.gov/publications/files/financial-stability-report-20250425.pdf>; The OCC's National Risk Committee. (2025). *Semiannual Risk Perspective*. OCC. <https://www.occ.treas.gov/publications-and-resources/publications/semiannual-risk-perspective/files/semiannual-risk-perspective-spring-2025.html>
- 19 Cybersecurity & Infrastructure Security Agency, National Security Agency, Department of Justice, Department of Energy, Environmental Protection Agency, Transportation Security Administration, Australian Signals Directorate, Australian Cyber Security Centre, Canadian Centre for Cyber Security, National Cyber Security Centre (Part of the GCSB), National Cyber Security Centre (part of GCHQ). (2024, February 7). *PRC State-Sponsored Actors Compromise and Maintain Persistent Access to U.S. Critical Infrastructure*. Joint Cybersecurity Advisory. [https://www.cisa.gov/sites/default/files/2024-03/aa24-038a\\_csa\\_prc\\_state\\_sponsored\\_actors\\_compromise\\_us\\_critical\\_infrastructure\\_3.pdf](https://www.cisa.gov/sites/default/files/2024-03/aa24-038a_csa_prc_state_sponsored_actors_compromise_us_critical_infrastructure_3.pdf)
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- 27 Cybersecurity and Infrastructure Security Agency. (n.d.). *CISA Artificial Intelligence Use Cases*. <https://www.cisa.gov/ai/cisa-use-cases>
- 28 OCCIP is responsible for coordination of Treasury's efforts to enhance the security and resilience of the financial services sector's critical infrastructure. The office works closely with financial sector companies, industry groups, and government partners to share information about cybersecurity and physical threats and vulnerabilities, encourage the use of baseline protections and best practices, and respond to and recover from significant incidents.
- 29 G7 Cyber Expert Group. (2025, June 20). *G7 CEG Reconnection Framework Best Practice*. Treasury. <https://home.treasury.gov/system/files/216/G7-CEG-Reconnection-Framework-Best-Practice.pdf>
- 30 Previous versions of this recommendation also highlighted the need for expanded supervisory and enforcement powers for NCUA to monitor the risks posed by third-party service providers to its regulated entities; however, NCUA has determined that it may have sufficient authority to monitor these risks through information sharing agreements.
- 31 There are numerous examples of U.S. regulators applying "gold-plating" to internationally agreed upon capital standards, which hold U.S. institutions to higher standards than international peers.
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- 134 S&P Global Market Intelligence LLC. Data as of June 30, 2025; NAIC. (2025). *2024 Annual Property & Casualty and Title Insurance Industries Analysis Report*. <https://content.naic.org/industry/insurance-industry-snapshots-analysis-reports>; The 10.4 percent figure from S&P is based on insurer-reported premiums from regulatory filings across states, whereas the 14 percent figure from ICE referenced in Section 4.1.5 is derived from loan-level data on payments made by mortgaged homeowners.
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