

2024 UNC Banking Institute
March 28, 2024
Outline of Presentation

Title: A Non Zero Game – How Increased Interest Rates Are Impacting Capital Markets and Investment Banking

Moderator: Edward P. O’Keefe

Panelists: Grovetta Gardineer, Senior Deputy Comptroller for Bank Supervision Policy
Jywanza Robinson, Senior Examiner, Federal Reserve Bank of Atlanta
Edward Ivey, Head of Derivatives, Moore & Van Allen
Paul Kurzeja, Associate General Counsel, Bank of America

Summary: Panel will discuss how exiting the prior “zero interest rate” environment and operating in today’s market have presented new regulatory and commercial risks for capital markets and investment banking. The panel plans to cover a broad range of topics for a sense of how regulators and the market are thinking about how this new interest rate environment has introduced unique concerns, including those related to competition for deposits, credit risk on existing loan portfolios, new requirements for new loans, securitizations and hidden losses on balance sheets of customers and their financial institutions.

Presentation:

Introduction – *Ed O’Keefe* (10 minutes)

After the Financial Crisis, interest rates across all tenors and credit types began a decline. The result was a period of many years in which net rates after inflation were at zero or negative. The phenomenon occurred across markets and countries. Many factors drove the decline, including monetary easing, list factors.

The Pandemic initially continued the decline, with rates dropping as economic activity slowed. In response, multiple governments engaged in aggressive monetary stimulus. The stimulus included direct grants, forgivable loans and increased benefits, such as unemployment. The result was an increase in the money supply, which with the easing of the pandemic, led to a significant increase in economic activity. Deposits rose sharply, with bank’s asset liquidity growing over 60% from year end 2019 to year end 2021.

The result was as sharp increase in inflation. The Federal Reserve responded with increased interest rates, leading to a rapid increase in core interest rates. The speed of the increases challenged and continue to challenge the financial industry. For example, while the equity markets accelerated to record highs, the bond market had an epic bear market, with the greatest single year decline in over 250 years.

The Effect on Banks – *Grovetta Gardineer and Jywanza Robinson* (20 minutes)

- Background
 - Historical Review and Background
 - Banking Industry Prior to 2023
 - Low Interest Rates, High Liquidity
 - Regulatory Perspective
 - Interest Rates Will Rise, Plan for It
 - OCC Semi Annual Risk Perspective
 - Issued in Late Spring and Late Fall^{1 2}
 - Other Regulatory Guidance
 - The Events of March 2023
 - An Event, Not a Catastrophe
 - Contagion Managed
 - Role of Social Media (Slack)
 - Lessons Learned
 - Risk and Control Systems and Procedures
 - Forward Looking Perspective
 - Understand Customer Base
 - Risk Layering
 - Assumptions
 - Contingency Funding Plans
 - Assumptions
 - Liquidity Flow Projections

¹ <https://occ.gov/publications-and-resources/publications/semiannual-risk-perspective/files/pub-semiannual-risk-perspective-fall-2022.pdf>

² <https://www.occ.gov/publications-and-resources/publications/semiannual-risk-perspective/files/pub-semiannual-risk-perspective-spring-2022.pdf>

- Fintech Arrangements and Effects
- Managing Social Media
- Alignment Among Regulators
- Prior to March 2023

The Effect on the Commercial Lending – *Ed Ivey and Paul Kurzeja* (20 minutes)

- Depends Upon the Transaction
 - Large v. Small Borrower Deals
 - Floating Rate v Fixed
 - Regional Variations
- Commercial Real Estate – What is It?
 - Office Building
 - Retail
 - Warehouse
 - Multi Family
 - Collateral for Business Loans
- Managing Loans Under Stress

The Future – *Grovetta Gardineer, Jywanza Robinson, Ed Ivey, Paul Kurzeja* (20 minutes)

- Individual Bank Stresses
- Regional Challenges and Opportunities
- Capital and Risk Management Activities
- Economic Growth and Regulatory Paperwork Reduction Act Review
 - Third Iteration Starts 2024

Q&A (5 minutes)