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Department of Financial Institutions

Bluegrass Community Bankers Association's Annual Conference

Kentucky Department of Financial Institutions

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Discussion Topics

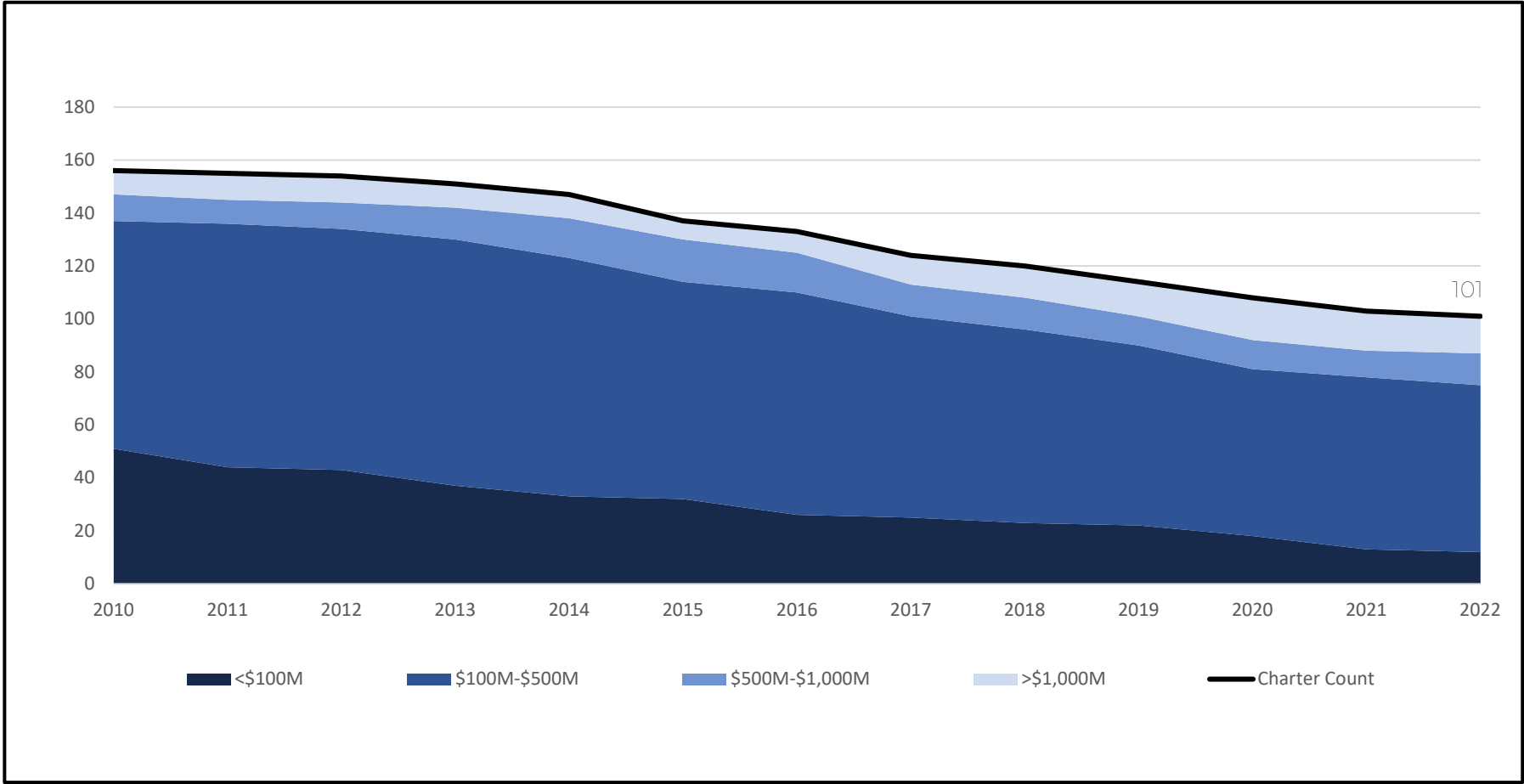
- **Industry Trends**
- **2023 Exam Priorities**
 - Liquidity
 - Interest Rate Risk
 - CECL
- **DFI Operations**

Kentucky Bank Performance

	YE2018	YE2019	YE2020	YE2021	YE2022	1Q2023
# of Banks	120	114	109	104	101	100
# of Banks <\$100 million	23	22	18	13	12	11
Total Assets (millions)	\$51,870	\$53,280	\$61,360	\$65,453	\$64,348	\$66,067



KY Banks by Asset Size



Kentucky Bank Performance

NIM – Net Interest Margin
 ROAA – Return on Average Assets
 ROE – Return on Equity
 CAP – Tier 1 Leverage Capital Ratio

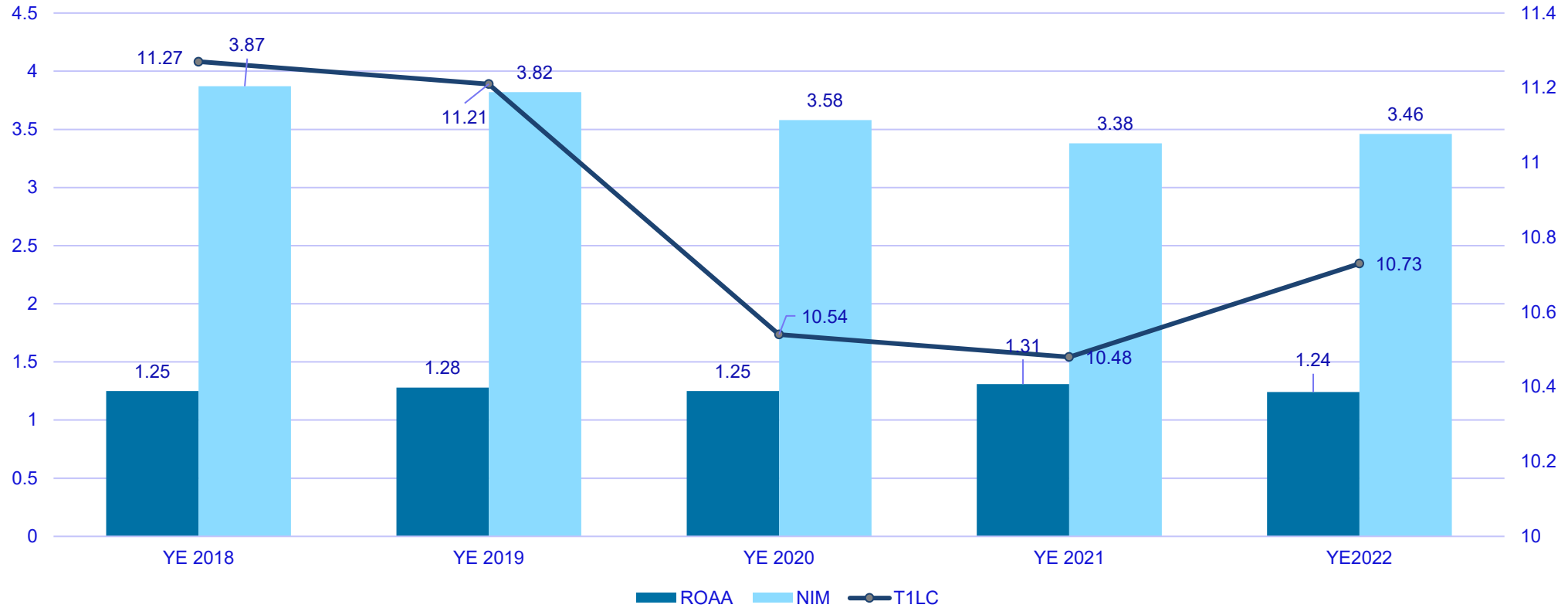
12/31/2022	# BANKS	NIM	ROAA	ROE	CAP
National	3,733	3.09	1.16	12.30	9.41
Kentucky	101	3.46 #4	1.24 Tied #5	12.76 #3	10.73 Tied #1
Illinois	272	2.29	1.07	11.29	9.03
Indiana	73	3.35	1.38	14.20	10.22
Missouri	201	3.33	1.38	15.88	9.42
Ohio	106	3.56	1.29	11.54	10.34
Tennessee	111	3.39	1.25	11.99	10.05
Virginia	48	3.50	1.24	9.98	10.73
West Virginia	38	3.53	1.15	9.50	10.07

*Figures above represent weighted averages.



KY Bank Performance

Bank Financial Metrics





Kentucky Bank Performance

- Average loan growth during 2022 = 14.6%
- Asset quality improvement
 - Average past due ratio
 - YE2019 = 2.04%
 - YE2022 = 1.01%
 - Average Texas Ratio
 - YE2019 = 7.22%
 - YE2022 = 3.57%



2023 Exam Priorities

- Liquidity
 - Average on-balance sheet liquidity declines
 - YE2021 = 28.5%
 - YE2022 = 21%
 - Large unrealized losses hinder access to liquidity
 - As of YE2022, average unrealized loss on AFS securities totals \$15.8 million
 - Review and monitor liquidity sources outside of securities portfolio
 - Test access to funding lines, especially unsecured lines
 - Review CFP and stress scenarios
 - Establish access with Discount Window and BTFP



2023 Exam Priorities

- Interest Rate Risk
 - 2022 brought about the sharpest rise in rates in 40 years
 - Average long-term assets/total assets ratio at YE2022 = 44.5%
 - Longer durations amplifying risk to capital and earnings
 - Review model assumptions
 - Discuss any policy exceptions and strategies to reduce excessive risk positions



2023 Exam Priorities

- **Current Expected Credit Losses (CECL)**
 - January 1, 2023 implementation date for banks with 12/31 FYE
 - Day one adjustment to capital made as of January 1 through retained earnings
 - Allowance for credit losses (ACL) used to measure provision needs going forward
 - March 31, 2023 Call Report is first regulatory reporting date
- **Examiners are looking for:**
 - Good faith effort to implement standard
 - Documentation
 - Discussion in meeting minutes



DFI Operations

- Still employing hybrid exam approach
 - Transaction testing and some discussion with management will be done onsite
- Staffing
 - Acting Commissioner and Acting Deputy Commissioner
 - Eight bank examiner openings across state



Statutory Reform

- Legal Lending Limit statute – KRS 286.3-280
 - Language changes passed in 2023 session, effective 6/29/2023
 - Only excess over 20% of capital and surplus must be secured
 - Codifies bank's ability to elect national limits
 - Other requirements from parity letter remain intact
- Additional Statute Reform
 - Department conducting review of all banking statutes for modernization