



Transcription

CSBS | STATE OF THE SYSTEM | DR. THOMAS SIEMS | NATHAN ROSS

Episode Transcript

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Nathan Ross (00:00):

Deposit insurance reform, it always comes down to who's going to pay, what's the cost associated with that? That's one of the major hurdles and everyone tries to pass on that question and so, well, we should do this, but we'll leave the funding aspect, but who's paying for it? Open for that conversation for another day? I think the other thing that's relevant here is of course, this requires congressional action and deposit insurance reform. It may not fall in the top 10 things that Congress needs to do, but the fact that there's legislation that is bipartisan, that is meaningful, that's not nothing.

Kyle Thomas (00:42):

You are listening to State of the System, the podcast that brings clarity and perspective to financial regulation. Welcome to State of the System where we explore the most pressing issues in financial services. I'm your host, Kyle Thomas. Today we're diving into the results of the 2025 CSBS Annual Survey of Community Banks. This survey now in its 12th year provides a unique window into the challenges and opportunities facing community banks nationwide. How community bankers view the economy and their business prospects is very important for policymakers, regulators, and ultimately consumers. In the past decade, more than 2000 community banks have closed, a shift that has deeply affected local communities, particularly in rural areas. Yet community banks play a very important role in our economy. Despite holding only about 11% of US banking assets, they provide 37% of small loans to businesses and 63% of agricultural loans. Every time a community bank closes, we lose access to local banking and some of the diversity that makes our financial system so strong. So that's why the survey exists and that's why we're going to be talking about it today. I'm thrilled to be joined by Tom Siems, Chief Economist for CSBS, and Nathan Ross, Vice President of Policy for CSBS, who's going to go through the what, the so what and the now what with regard to the survey. Guys, thank you for being here.

Dr. Tom Siems (02:10):

Thanks for having us. Yeah, great to be here.



Kyle Thomas (02:13):

So I think, Tom, I'm going to start with you because before we talk about what's in the survey, we probably just need to talk about the survey. So maybe in a few short words, give us a little perspective on why the survey was created, where it started, and how it's going.

Dr. Tom Siems (02:28):

Yeah, the survey helps us to really understand the concerns that community bankers have gives us a window of what's going on in their world, and every year we change the questions a little bit because the issues evolve, but we want to know what are those opportunities and obstacles that community bankers currently face.

Kyle Thomas (02:50):

Yeah, and when we say community bankers, for those who don't have a keen eye on the US financial services system, paint us a picture of a community bank who might be filling out this survey.

Dr. Tom Siems (03:01):

Yeah. Well, the community bank is under 10 billion. We don't have any banks that are larger than 10 billion. In fact, I think some 70% or so of the banks are between 1 billion and 10 billion in the survey this year. And so they serve their local communities. They're generally smaller institutions that are in rural areas. You have a lot of ag bankers and their relationship-oriented banks.

Kyle Thomas (03:30):

Perfect. And going back probably multiple years, CSBS started focusing its policy and advocacy on that segment, not to ignore the other segments of financial services, but we did that because we recognize that there's a unique business model here and that business model faces different threats and maybe has different opportunities than the other ones. So this survey kind of feeds into that policymaking process. So Nathan, how does this inform your work? Generally high level, where do you take these findings, these numbers, and how does it shape the work that you and your team do?

Nathan Ross (04:01):

That's a great question. We use feedback from the bankers in the survey in our regulatory policy making work, use data from the bankers, whether it's on their business prospects or the cost of compliance with various regulations to advocate for sensible changes to regulation and to policy that supports the community bank and relationship banking business model. We'll do



that by going up to Capitol Hill. Tom will talk to policymakers in Congress about the findings and what that means and what we can do to preserve and promote community banking in the United States. One thing that we have been doing in particular this year is working with the federal banking agencies around the cost of compliance and highlighting specific areas in the survey where community bankers feel the biggest pinch, where's the cost? Does that cost meet the benefit associated with that regulation? And that's one of the ways we're using the survey.

Kyle Thomas (05:06):

Perfect. What's the coverage look like on this thing? Just roughly how many states are represented in it? Is it a kind of a coast to coast thing, just roughly what's the landscape?

Dr. Tom Siems (05:17):

Yeah, so this year we had 268 community banks that completed the survey. That's about six point a half percent of the overall population of community banks responses came from 32 states, and like I said, most banks had assets between 100 million to 1 billion.

Kyle Thomas (05:37):

Excellent. Okay, so good background, kind of understand how, let's jump into the results for this year. Tom, I'll start with you maybe from kind of the 30,000 foot level, what are the big storylines or a couple of the big storylines that jumped out at you as someone who's been looking at this survey year in year out?

Dr. Tom Siems (05:55):

Yeah. Well, we've been doing the survey, like we said, going back to 2014, and this year is unquestionably characterized by uncertainty. We had a lot of economic uncertainty, particularly during the survey period, which was between April and July of this year. We had the changing tariff rates and swings and net exports and so forth, and that really had an effect on economic growth and consumer and business sentiment. So it was kind of a unique different world for the bankers. Yet at the same time, we found in the survey that there's some optimism about regulatory burden and potential for easing there, but there's some pessimism about the overall trajectory of the US economy. So for example, regulation was parentally kind of one of the top external risks faced by community bankers and talked about in previous years, but it ranked sixth this year, and that was down from first in survey last year. So that was a big change. Cybersecurity concerns or risks continued to be a top internal risks facing the bankers. That's closely followed by technology implementation and costs. And interestingly, credit risk replace liquidity risk as the third most recently or frequently cited internal risk. And so there's a lot of



other interesting information in there. Every year we add some special questions, and this year we had some special questions on deposit insurance reform and also on bank fraud.

Kyle Thomas (07:33):

So I got a little sneak peek at the survey results, so I scanned through it quick and some things that jumped out at me. One was the top item on the banker's lists of concerns or external risks were the top two I guess were around net interest margins and core deposit growth. So I wanted to give those a little airtime. What do you think is driving that, either Nathan from the policy perspective side or Tom as you're reading the results and maybe some of the more anecdotal information in the survey, maybe on net interest margins, we're in a different rate environment than we had been in the previous 10 years. How's that translating into the banker's sentiment and why do you think that maybe elevated that risk?

Dr. Tom Siems (08:10):

Yeah, the interest rate environment has been really challenging, particularly since the pandemic short-term rates going down, and then we had the inflation period and short-term rates went back up, and now they're coming back down a little bit and we had a long period there, some 22 months or so of inverted yield curve really hard for a bank to manage the net interest margin, particularly during those times. So it's no surprise that net interest margins was up there at the top risk. In fact, out of the survey, I think it was 88% of the respondents said that that risk was either extremely important or very important.

Kyle Thomas (08:48):

Interesting. And so a close second there was core deposit growth and it's likely these two things are related, I would suspect, but what do you think is driving some of the concerns, Nathan, on the core deposit growth? Why do you think about 80% of banks rated that extremely important or very important in the survey?

Nathan Ross (09:07):

Yeah, the policy environment questions associated with deposits right now. I mean, I think ever since SVB, Signature back in 2023, it's brought to the fore concerns by particularly community bankers, but also the broader banking industry about what should deposit insurance coverage look like. For example, there was the systemic risk exception that covered all deposits for a brief amount of time, but we saw a lot of deposit movement from community banks to the largest institutions during that period in early 2023 because depositors, uninsured depositors felt like, I need to make sure my money is parked in an institution where it's going to be safe. If that institution fails, the federal government is going to step in and back all of my funds. That is



not a big picture, an environment we want to have related to deposits. We want small businesses, for example, to be able to feel comfortable that their money is safe at a community bank as well, that they don't need to go to the largest institutions for there to be that level of certainty.

(10:13):

There have been conversations in DC of course, about that just right now there is legislation that is being contemplated, discussed, introduced related to raising deposit insurance coverage limits for certain types of business transaction accounts. Those things have to work themselves out. That's not a fast process, but the point is, this is a key area of concern for bankers and particularly community bankers around, is my core funding going to walk out the door and go to a large institution because those funds are protected there, but not at my bank. There are also new competitors. I mean, we just saw at lightning speed, a new stablecoin framework passed into law this summer. So bankers are concerned about the competitive landscape related to deposits. Will there be a deposit outflow into new payment instruments, namely stablecoins here, we don't know what that's going to look like. We're still, the regulations haven't been written, but there are certainly concerns about how are we going to keep core deposits in the banking system going forward.

Kyle Thomas (11:22):

So just to pull on that a little bit further is we're keeping a close eye obviously and are very engaged in the stablecoin, tokenized deposits, digital assets, evolution as we are seeing happen right now. But from a banker's perspective, the threat as I see it is that a consumer may find that in the future, a stablecoin type vehicle for transactional activity is just easier, cheaper, faster, and then they'll just hold funds outside of the traditional system to transact. And today those are core deposits. Those are a bank's funding sources and are so important. So that's almost certainly driving some of this elevated concern. I wonder also about things. A lot of the community banks are headquartered or located or operate in pretty rural areas, not all of them. We have many urban community banks, but areas that may not be seeing significant population growth or economic activity.

(12:18):

So that depopulation, I'm from Iowa. I know that that is the case in some communities in Iowa and a trend out there is that the generational wealth transfers that are happening from the farming families to the next generation when the kids may not be there anymore. So do those funds leave the bank and then couple that with the threats facing these institutions from



stablecoin and digital assets and also just the kind of challenges of operating in a low growth environment contribute. Another kind of macro trend that I'm curious about if it came through in the survey results at all, Tom, is about how inflation is popping up in this and what community bankers sentiments are around inflation.

Dr. Tom Siems (13:00):

Yeah, we've been asking bankers about their concerns on inflation over the last couple of years just because inflation has been more in the news the last couple of years. But the thing about inflation is it's really, it's kind of a personal thing, and what I mean by that is that every individual and probably every business entity out there has a different inflation rate because we don't all buy the market basket of goods that's used to compute inflation. And so prices go up for some things and it impacts one consumer or one business, but it has no impact on another. This is why the Fed really tries to bring down the overall inflation rate down to some lower level, but it's been elevated in recent years and at about 2.6% currently the Fed's preferred inflation target. There of course is 2% and it's still an issue.

(13:53):

When we asked community bankers about that, they said that deposit costs was most impacted by inflation, although the share of respondents that cited the concern fell from 59% last year to 46% this year. The second most impacted by inflation was personnel expenses, and 23% of the respondents said that, and then operating expenses outside of personnel was also impacted. 19% of respondents said that, and that was up from 8% last year. Even with all that though, there's 75% or so of the respondents say that it's manageable. The inflation environment right now is something that they can manage, but it does impact them.

Kyle Thomas (14:39):

And really on both sides. So from the deposit side, which is the bank's funding source, intuitively you would expect people would kind of demand a higher return on the savings that they have in a bank if we're in an inflationary environment.

(14:52):

And then on the other side, their operational costs go up because the people who are working at a bank, which are businesses are demanding higher pay and to keep up with inflation. So it is squeezing them from both sides of the coin, but interesting to see that it's still manageable. Anything from a maybe more regional or specific markets standpoint that is noteworthy from an inflation side of things? I'm thinking in terms of there's winners and losers in an inflationary



environments, prices go up. Maybe what we're seeing in the beef market, for example, prices are going up. Let's go back to Iowa. Yeah, yeah. Can speak a little personally on this, prices go up, it's good for some, but it's bad for others. So did that come through at all in the survey results?

Dr. Tom Siems (15:31):

So it doesn't come through, but in terms of things weren't identified in the survey, but there are clearly some institutions that face a tougher inflation environment because maybe they're in the beef or they're not into that, into some other commodities that move at different rates. I think one of the areas though that you can really see the impact is that housing, it's always location, location, location on housing and housing prices and costs are going up nationwide, but they go up more rapidly in some areas than they do in others. And so it comes through for sure, but the extent of kind of understanding the ins and outs and the actual specific price increases or commodities, we didn't get into that detail.

Kyle Thomas (16:18):

Yeah. Well, so I mentioned banks or businesses, and so they have internal things that they have to manage and operate, and these things translate into costs, and we talked about some of these things in the survey results. I'm thinking about some of the more internal risks and concerns around cybersecurity preparedness, cybersecurity, posture, as well as technology and the costs of implementing new technology. Everybody's talking about artificial intelligence, that's a new technology that's affecting not just banks, but any business out there. The survey results, those are top of the list, not number one or number two, but probably three and four, and they're very high on the list. Nathan, kind of to the work you and the team are doing around some of the policy and supervisory processes around some of these things, what can you say about how we're thinking about cybersecurity, making that environment workable for banks also around technology and the implementation of new technology for these community banks?

Nathan Ross (17:17):

I'm glad you asked an easy question, Kyle, how are you solving all of our problems? That's right. So it is always top of the list as far as risk go, right? Cybersecurity, it is the threat and the risk that is never going away, unfortunately. So what we've been doing, what the states have been doing, state regulators is really working over the past several years to raise the level of awareness around what you need to do to protect your institution, the responsibilities that are yours. As an executive team, as a board of directors, I'm thinking of our Ransomware Self-Assessment Tool that is specifically targeted to executive management and boards of directors. I think that's a really great tool to help them level set when they think through, we're going to



onboard a vendor, for example, who's going to help us protect from our protect cyber posture, or we're going to bring in another vendor to partner with us on providing a new product or service.

(18:16):

That kind of tool is really good. Again, for that executive, the executive C-suite, we also have a Cyber Hygiene Campaign that gets, I think, further down into the weeds and is more on an ongoing basis, what should you be looking for as you run the day-to-day business, right? That's things like inventory management end of life for your technology and your assets at an institution. Multifactor authentication, I mean, all the things that we think of down several layers that translate into a more protected institution. We're rolling that out through the states, through state regulators as they work with their institutions. I think one of the things I think you asked at the beginning or said, we're going to talk about the so and now. I think one of the things we've been seeing from a supervisory standpoint is that there may need to be a fundamental rethink and reset on how cyber supervision occurs in the banking industry, particularly for community banks, the largest institutions, they absolutely have huge cyber risk. They also have massive teams dedicated and the resources that they can deploy to effectively defend against those risks. I'm not trying to downplay the risk, but I think the smaller institutions we have seen from a supervisory standpoint probably need the most backup here. One of the things that we're working on as state regulators go out into the field and look and partner with institutions in the exam process, how can we make our supervisory practices more helpful for them to combat this risk?

Kyle Thomas (19:52):

When I'm not hosting podcasts in my spare time, I also work on regulatory and supervisory issues relevant to banks and non-banks. So in that work, I do talk to some bankers and even some smaller non-bank financial service companies. And what they say is that the technology environment is changing really, really quickly, and we need the ability to take advantage of these new technologies because some of these new technologies like artificial intelligence and fraud detection actually will help us more cheaply and more effectively manage our cyber risk. But we need good regulatory frameworks and good expectations to engage with these third party vendors, to engage with the private industry, to figure out where the good tools are and how they can really help us manage our risks. So I think as a group of regulatory policy people, we can put some work into thinking around how to provide clearer paths for engaging with third party vendors, for example, a hundred percent how these relationships differ between the types of services that these companies are providing. Because if you're a small bank, to your point earlier, these large banks have on staff dedicated teams to managing a lot of these risks. If you're a small bank, you can't afford to have all these people dedicated to one function. There's



a lot of jack of all trades in community banking, and so you have to rely on your outside vendors to do some of this stuff for you. And I think our approach as regulators could respect that.

Nathan Ross (21:14):

Yeah, absolutely. I think guidance needs to be more than just big picture here. Here we need something that's more operational. If you are going to engage a vendor, for example, on deposit gathering or for payments, whatever it may be, there needs to be for institutions to feel more comfortable from a cyber perspective, but also an ongoing compliance and risk management perspective. More again, operational clear rules of the road and expectations. What are the risks they should be looking for, how to mitigate those risks. That would be, I think, a key thing for the industry.

Kyle Thomas (21:48):

Yeah, absolutely. Kind of along these lines, we asked some other questions in the survey around, we touched on deposit insurance reform and some of the driving factors there. Maybe we'll explore fraud a little bit. So in the survey, this is also something that pops up on their list of threats concerns. What about this year? How were the results indicative of the fraud environment out there?

Dr. Tom Siems (22:11):

So we asked them about fraud and the community bankers were surveyed on the various types of fraud that they experienced in their institutions, and they reported the highest incidents of credit and debit card fraud. 59% of reported fraud cases were attributed to credit and debit card fraud. The second most common type of fraud that they identified was check fraud 17%, and then 12% of fraud cases were identity theft and account takeovers. So we also asked about, well, what are your dollar losses in these areas? And the highest was the credit and debit card cases. 39% of reported losses came from that type of fraud check fraud accounted for 30% of reported losses and identity theft in account takeover resulted in 11% of losses among the respondents.

Kyle Thomas (23:06):

Interesting. And fraud losses are right off the bottom line. So if there's a loss and a consumer has to get restored, that's directly off the bottom line. It also makes me think back to our previous conversation around the opportunities right now with technology to kind of combat that, but also the reality that all those technologies that are improving in their ability to combat fraud cost money for the banks, but also those technologies can be used to perpetrate fraud. And so I think that just kind of goes back to the comment you made, Nathan, around the work



that we're doing internally to kind of help banks protect themselves, educate consumers. That's another big role of state regulators too, is educating the consumer base out there on some of these trends.

Nathan Ross (23:48):

Yeah, the states have done a lot of work here to educate consumers, to your point around fraudulent schemes, whether it's elder financial abuse, I'm thinking of in particular, not to pick favorite states here, but I think Washington Department of Financial Institutions had a great cyber, excuse me, fraud campaign, anti-fraud campaign for their residents, several other states as well. I mean, this is something where they are working really hard to make sure that consumers know what the risks are because it's pernicious. It is everywhere. It's a sophisticated, is sophisticated environment where it's very easy to be taken advantage of. And I think that requires a whole of government, whole of industry, not just the financial services industry, retail, I mean, you name it. There are so many actors here that it leads to, frankly, some of the problems of addressing fraud.

Kyle Thomas (24:41):

No, I think that's right. And that was one of the more forward looking elements to the survey. There's not a really clean way of segueing into the deposit insurance reform discussion, so I'll just do that. But I know another forward looking question or a set of questions we ask is around deposit insurance and how bankers, particularly these community bankers are feeling about deposit insurance reform. So I wanted to explore that a little bit more. What did, what did the bankers say about this and where their aspirations are with deposit insurance reform? And then Nathan, I'll maybe hand it over to you to kind of talk about what's in play.

Dr. Tom Siems (25:16):

Survey says 79% of the surveyed community bankers said that they would alter the current deposit insurance framework. The most common solutions were Targeted Unlimited Coverage and increased coverage. Targeted Unlimited Coverage would consist of unlimited coverage to certain account types and the limited coverage to others, such as non-interest bearing transaction accounts. And so interestingly, under increased coverage deposit, insurance limits would be raised from the current \$250,000. The majority, which is 72%, favored a new limit of \$500,000. Well, 21% would raise the limit to \$1,000,000 and 7% would put the limit somewhere between the current amount and \$500,000.

Kyle Thomas (26:05):



Interesting. So kind of in summary, broad consensus, that limits need to be moved up in these survey responses and exactly to what level is subject to debate. I'm old enough to remember, and back to my bank, examining days, all the plaques at every single teller window had your deposits insured up to \$100,000. And that had been that way. And at that number for a long, I remember 25,000, oh geez, let's not date each other, but I mean, a hundred thousand persisted for a long time. And that was just kind of in the public mindset, was that up to a hundred thousand and then it moved to 250 in the financial crisis period, and it stayed there ever since. But we've now been in an inflationary period. We've gone through a lot of economic growth through the last 15, almost 20 years at this point. Where are the winds blowing Nathan on deposit insurance reform, and what are some of the hopes that we're starting to frame our thinking around?

Nathan Ross (27:02):

Yeah, so number one, the results of the survey, not surprising based on everything we just talked about, there's been a lot of desire to move up deposit insurance coverage limits, particularly among community banks because they want to keep those customers, primarily small business customers that they want to lend to. They want to have a robust lifecycle relationship with them. They want to lend to them. They want to manage their funds in a deposit account, so on and so forth. So again, not surprising the results here of the survey. I think where it's going, I think the FDIC for example, did some work on this right after the 2023 banking turmoil where they threw out a handful of different options for potential reform. And they said raising coverage limits for certain types of transaction accounts makes sense. I think that has been the most widely viewed as potential reform options go.

(28:04):

What could happen? I think, again, there's some legislation that's floating out there that would do just that, that would raise deposit insurance coverage for business transaction accounts while keeping it more or less the same for retail deposits for other types of deposit accounts. I think the trick is with deposit insurance reform always comes down to who's going to pay, what's the cost associated with that? That's one of the major hurdles, and everyone tries to pass on that question. It's not comfortable, and so, well, we should do this, but we'll leave the funding aspect, but who's paying for it open for that conversation for another day? I think the other thing that's relevant here is, of course, this requires congressional action and the deposit insurance reform. It may not fall in the top 10 things that Congress needs to do. When you think about funding the government, having a defense bill passed every year, other major policy issues that are outside of banking and financial services. It's just hard to get time on the congressional calendar on the floor calendar. So I don't know what the prospects are, but the



fact that there's legislation that is bipartisan, that is meaningful, that's not nothing, let's put it that way.

(29:21):

So we'll see. There's definitely some more twists and turns here, but I would not be surprised if this conversation of course continues. The other thing I would mention very briefly, you talked about the limit being 250, right? Set back in Dodd-Frank. There has been more conversation over the past several months about these static thresholds, whether they are baked into a particular regulatory requirement or deposit insurance coverage about does it make sense going forward to recalibrate those, let's say move them up based on economic growth and inflation and then to index them going forward? I don't know if we'll see that in the deposit insurance space. I think there is more openness to that than there has been probably in the past where you would hardwire it at a hundred thousand or 250,000 and just leave it for a decade plus. I think there is more recognition that these things should move as the economy moves.

Kyle Thomas (30:18):

Perhaps a good set of questions for the 2026 annual survey.

Dr. Tom Siems (30:22):

Yes.

Kyle Thomas (30:23):

Yeah. Well, I think that last discussion really highlights the importance of getting this information from this segment of the banking and financial services industry because as these policy debates are being kicked around Washington, like deposit, insurance reform, or name your topic, we now have numbers behind it and we can say, this is how this industry feels about this particular issue. And if something with deposit reform, it does not affect community banks the same way it affects the big banks. And so their specific perspective is super important to have in a body of work like this. So Tom, Nathan, really appreciate you giving us the what, the so what and the now what on the annual survey results. Look forward to having you back maybe next year. Alright, thank you.

Dr. Tom Siems (31:03):

Thanks Kyle.



Kyle Thomas (31:05):

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