



Highlight of the Week

The Fed Releases Stress Test Scenarios

- The Federal Reserve recently released scenarios for the 2024 supervisory Dodd Frank Act Stress Test (DFAST). Thirty-two large lenders (all the category I-IV banks) will participate and be subject to the resulting Stress Capital Buffer ('SCB') or capital limitations.
- Previous tests failed to predict stresses (both systemic and of individual institutions) in the Spring of 2023. To help understand and avoid a similar situation, the Fed has added exploratory scenarios to mimic the challenges of 2023 including:
 - 2 exploratory macroeconomic scenarios, which simulate funding stress, rising interest rates, and a global recession.
 - 2 exploratory market shocks, which require banks to simulate defaults of their five largest hedge fund exposures.
- As usual, this year's stress test will include:
 - One baseline scenario
 - One severely adverse scenario that simulates a severe macroeconomic global recession characterized by significant declines in real estate and corporate debt markets. This scenario is comparable to the severely adverse scenario published for 2023, with a slightly more pronounced fall in equity prices.
 - One global market shock scenario that only applies to banks with significant trading activity. This scenario is slightly more drastic than the comparable scenario published in 2023, especially regarding equity prices and treasury rates.
- Stress tests, which are constructed based on past events and the 2008 financial crisis scenarios, have not recently affected bank market prices and perception. However, this year's tests may draw more attention due to the three bank failures in March 2023, as well the current focus on increases in capital requirements under Basel III.
- The Fed plans to release stress test results (at an aggregate level) in June, which may certainly affect large banks' regulatory discussions on the necessity of proposed increases to capital requirements.

Rate Curves

