

# 2024 Annual Report

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## MISSION:

“Everything we do is driven by and revolving around the soundness, safety and stability of the banking system.”

## VISION:

“Our vision is to ensure and maintain trust and confidence in the banking system by the public (our Mission) by being innovative, effective, efficient, fair, friendly, firm, and consistent in rendering and availing the right and appropriate financial and banking regulatory and supervisory supports, tools and services.”

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## SUMMARY ASSESSMENT

The overall condition of the FSM commercial banking sector remained satisfactory for the year, December 31, 2023 – December 31, 2024. Growth and stability still maintained.

- Total Assets of the banking system increased by \$29.238M from \$477.166M to \$506.404M.
- Asset quality for the banking system for the year remains satisfactory. The industry ratio of Non-Performing Loans (NPLs) to Total Loans stood at 0.67% at year end, compared to 1.57% for same period in 2023. The volume of outstanding loans decreased from 2.55% to 1.32%. However, provisions for Bad Loans to mitigate against potential losses remain more than adequate at \$2.529M, about two times the sector's volume of NPLs.
- Consumer lending increased from \$35.996M to \$38.660M, while commercial lending decreased from \$48.019M to \$44.040M. Deposits increased from \$424.449M to \$453.333M, primarily due to increase in savings, time and other deposits. Demand deposits constitute 40%, while Savings deposits represent 51% of the total Deposits.
- Return on Assets decreased from 3.34% to 3.03% over the year, primarily due to the lower yields on the excess liquidity placed abroad in US deposits and investments. Invested funds as percentage of total assets is roughly 80.3% over the year.
- The system remains highly liquid, \$406.874M or eighty percent (80%) of the sector's \$506.404M total assets are liquid assets which are placed or invested abroad.
- In aggregate, approximately \$411.832M of the sector's \$506.404M total assets are liquid assets. The banking system continues to maintain reliable access to adequate sources of funds to meet anticipated local liquidity needs.
- The banking system remains highly capitalized, core capital and retained earnings maintained well above the required minimum capital threshold.
- Escheatment for year end 2024 was reported at \$120,385.26 of which \$600.00 was deducted by the regulated banks for publication fees. The total payment made to FSM Treasury was \$119,785.26.
- Net income realized for the year ended 2024 was \$14.573M.
- The two regulated banks still maintained FDIC deposit insurance coverage up to \$250K per deposit account.
- Of particular challenge before Banking Board is the staff not being able to attend FDIC Banking School since COVID-19. This is due to priority given to FDIC staff. However, we continue to work with FDIC.

## NEW DEVELOPMENTS

Similar to other banking system in other countries, the financial stability of FSM banking system is directly linked to both the domestic and global economic and technological circumstances.

### ***Climate Change:***

Climate change certainly has negative implications on the banking system if not mitigate properly. The risks of climate change can manifest themselves in the form of credit, market, and liquidity. Ways to minimize and/or mitigate such risks is a great challenge before the Board and the banking system. The global understanding shared by bank regulators and supervisors advocate for supplementary actions through modifications to various regulatory standards, such as Pillar 1 (risk weighted assets), Pillar 2 (supervisory review processes and capital add-ons capacity to absorb loss) and/or Pillar 3 (disclosure obligations) to help mitigate climate change and at the same time to minimize the impacts on the soundness, safety and stability of the banking system.

The Board continues to explore possible financing mechanism with DECEM, whereby Climate Fund could be established as seed funding either on a grant or guaranteed basis with minimal interest rate for borrowers who incorporate climate change mitigation strategies in their portfolios, for example, to relocate from shore areas to higher grounds due to sea-level rise, funding for housing projects that incorporate measures to mitigate climate challenges or impacts, i.e., solar energy, among others.

### ***Introduction of Basel III Framework:***

The prudential returns or Call Reports currently utilized by the Banking Board for compiling and analyzing financial and statistical data have been in place since 1980s. These templates need revisions in order to capture other information and new data due to the changes in risks, operations, technology and regulations. The IMF through PFTAC continues to assist the Board with prudential regulations, standards, returns or templates with instructions or guidelines, focusing on risk-based approach. The objective is to bring these important regulatory and supervisory tools up-to-date consistent with the acceptable global prudential practices. This is being approached on the Micronesian regional level with the Republic of Palau and Republic of Marshall Islands, although Palau and RMI are slightly ahead than the FSM in adopting some of introduced risk-based standards. FSM, Palau and RMI aim to adopt standardization or uniformity of prudential standards and returns as it will bring about transparency, consistency, convenience, efficiency and effectiveness in supervision of banks.

There are eleven Prudential Standards Bank Regulators and Supervisors employ to carry out supervision. IMF through its field office, PFTAC, is helping the Board with this effort. So far, four of the eleven Prudential Standards introduced in 2023 which are undergoing review and study. The objective is to update regulatory and supervisory standards in order to capture or extract additional financial and statistical data for strengthening the regulation, supervision. The four Prudential Standards are: (1) Governance and Risk Management, (2) Capital Adequacy, (3) Credit Risk Management, and (4) Liquidity Risk Management. IMF will field additional Missions focusing on trainings and workshops on each Standard. When staff is fully trained and familiar with the Standards, consultations and collaborations will take place with the respective banks. prior to promulgation.

**The Legal tender  
in the FSM is the  
US Currency.**

***Crypto, Digital Currencies and Virtual Assets:***

The legal tender in the FSM is the US Currency. However, crypto, digital currencies and virtual assets have been accepted in other developed economies as substitutes or alternative payments for goods and services. Advocates for these alternative forms of payments have expressed interests to penetrate FSM markets; however, FSM's legal tender is USD. Both banks in FSM have also expressed hesitations to deal with these forms of digital currencies due to potential risks involved. Presently, these alternate forms of payments are decentralized and not backed-up by any State, thus are not regulated. The advantage or benefits of these forms of payments is convenience and less fees; however, the risks are high and protecting public interest is equally important, i.e. safety, confidentiality, stability, among others. The Board believes FSM is not ready to entertain digital currencies and virtual assets as there is no legal framework in place for governing these alternative forms of payments.

***Mutual Cooperation's:***

The Board has established mutual cooperation arrangements with recognized bank prudential regulatory and supervisory authorities in the region, US and with other international authorities. The objective is to enhance capacity building, mutual cooperation, and sharing of information. FDIC Examiner School has not opened its enrollment to outside students since COVID-19 due to space availability. This is a challenge before the Board as it has been proven that attending FDIC School brings invaluable experience.

Meanwhile other options, such as IMF, WB, and others are being explored, although not as effective as FDIC School.

**The Board has established mutual cooperation arrangements with recognized regulatory and supervisory authorities in the region, US and other international authorities.**

***On-Site Examination and Off-Site Analysis and Monitoring:***

FDIC Financial and Soundness Examination Team conducted examination on our domestic bank on an annual basis. Commissioner and staff participate in these examinations as a matter of regulator-to-regulator mutual cooperation and for capacity building purpose. FDIC Consumer Protection Compliance Examinations are also conducted by FDIC once every five to ten years, depending on the off-site analysis. The FSM Bank was rated as #2 on the last Consumer Protection Compliance Examination by FDIC. The #1 rating is the highest.

Off-site monitoring, analysis, review, and evaluation are routinely conducted and are the core daily regulatory and supervisory responsibilities of the Board. The off-site aims to assess and determine the degree of compliance, safety, soundness, and stability of individual bank and the banking system.

***Technical Assistance (TA) on Legal Framework and Prudential Regulations:***

The Banking Board requested a Technical Assistance from IMF through PFTAC to assist with the review on a drafted application for domestic banks establishing office abroad office as authorized under Section 311 of the Bank Act.

IMF through PFTAC also fielded two Missions to the FSM for one week to provide trainings to FSM, RMI and Palau on credit analysis and liquidity. These trainings were meant to further assist the three countries to better understand the Standards mentioned above.

***TA on Financial Soundness Indicators (FSI) Technical Assistance:***

FSM Banking Board serves as the focal point for IMF Financial Soundness Indicators (FSI). FSI reporting template and instructions changed in certain respects so the Board requested and received a TA aimed at improving staff capacity in the collection, compilation and reporting FSI data in compliance with the revised/new FSI data templates. FSI data, if accurately reported and properly compiled, becomes an imperative tool for gauging the health and soundness of individual and consolidated financial institutions, thus the overall health of the financial system of the FSM or any country. It is therefore useful indicators of past and current financial health and soundness of the financial institutions, and of the corporate and household counterparts. Staff participated in one of the FSI trainings held in Fiji. More FSI trainings are expected in 2025, among other relevant and key training needs that are critical and essential to the regulatory/supervision of bank.

***AML/CFT:***

AML and CFT are important aspects for ensuring safety, soundness and stability of the banking system. The Board also provides oversight in these areas. The Commissioner worked with the US Department of Treasury, Division of FinCen to host an AML/CFT training in Pohnpei. Representatives from the banks, law enforcement, tax and revenue, among others attended. The Commissioner also worked with the Acting Secretary of Justice on reactivating the Financial Intelligence Unit.

***Banking Permit/License Applications:***

There was a query about obtaining a license to engage in banking business; however, the inquirer failed to file the application. The Commissioner also met with a digital currency inquirer about interest to establish its presence in the FSM.

***IMF Article IV Mission:***

The Banking Board met and worked with the IMF Article IV Mission on financial sector data and presentation on the overall performance of the banking system.

***Annual AFSPC Meeting:***

Annually, the Association of Financial Supervisors of the Pacific Countries convenes to discuss concerns and issues affecting the banking system in the region and at the country level. FSM was supposed to host the 2024 annual meeting of the Association of Financial Supervisors of Pacific Island Countries (AFSPC); however, due to lack of funding, PFTAC decided to have the Annual Meeting of AFSPC in Fiji. Our Bank Examiner and Bank Financial Analyst participated on our behalf. Timor-Leste will host in 2025 and FSM in 2026.

***Website:***

The Board continued to post and update information on its website, including but not limited to quarterly financials: [www.bankingboard.gov.fm](http://www.bankingboard.gov.fm). The purpose for creating the website is to help the general public.

## BACKGROUND & GENERAL OVERVIEW

The FSM signed a Compact of Free Association (Compact) with the U.S., entered into force on November 3, 1986, for fifteen years. Both parties to the Compact agreed to renew the Compact but for duration of twenty years, which came to expiration in September 2023. Again, both parties agreed on the third Compact. Similar to the Compact I and II, Compact III includes FDIC Insurance Coverage for Bank of FSM under Article XI, which subjects the Bank of the Federated States of Micronesia to compliance requirements under the US banking and related laws, regulations, rules, supervision and prudential standards.

The Board is required under the Banking Act to produce Annual Report which should provide the general description of the condition of the banking system and operation of the Banking Board. This Annual Report focuses on the year 2024; however, other parts of the Report will provide information on previous years for comparative purposes.

**On May 10, 1979, four of the Trust Territory districts (Yap, Chuuk, Pohnpei and Kosrae) ratified the Constitution of the Federated States of Micronesia. In 1980, the FSM Congress adopted the Banking Act and signed into law by the President as Public Law 1-94 codified under Title 29 of FSMC, as amended.**

Section 202 of the Act stipulates the principal purposes of the Board, generally:

- To undertake the licensing and supervision of banks;
- To protect the interests of depositors; and
- To promote the soundness, safety, stability, and development of the banking system.

In view of the above general mandates, the Board as the supervisory entity is charged with essentially the micro prudential policies of the banking system, ensuring regulated banks comply with the provisions of the Act, regulations and prudential standards. This involves activities relating to monitoring, inspecting, and examining banks to ensure adherence to the laws and regulations and that they operate and develop in a safe and sound manner for a stable banking system. Additionally, the Act grants authority to the Board to promulgate regulations for effective execution and implementation of the Act.

The “stability and development” elements of the mandate relate to the macroprudential policy activities for achieving and ensuring financial stability. In a nutshell, the overarching goal is to minimize probability of failure of banks by making sure the bank manages risks prudently, has plan in place to restore itself to financial and operational soundness in case of a shock, sufficient capital buffer to absorb losses while remaining viable, sufficient liquidity to meet obligations as they become due, among others. The Board in discharging its micro prudential responsibilities also helps to promote stability and resilience of the financial system and, through that, helps to contribute to the overall objective of promoting sustainable economic growth and healthy FSM community.

It should be noted; however, that the FSM’s legal tender is the US Dollar, thus technically speaking, certain macroprudential policy activities in respect to “stability” might be outside the Banking Board’s responsibilities. However, the FSM has enacted certain legislations, including the Consumer Protection



Act (P.L. 10-52) or Title 34, Chapter 2 which specifically cap the credit transaction interest rate at 24%. The average prevailing interest rate charged by the banking system in 2024 was 14.75% for consumer loans and 4.63% for commercial loan.

#### **Principal purposes of the Board**

- **To undertake the licensing and supervision of banks;**
- **To protect the interests of depositors; and**
- **To promote the soundness, safety, stability, and**
- **development of the banking system.**

There are several financial institutions in the FSM. Two of them fall under the supervisory purview of the Board, the Bank of FSM which is a domestic bank and the Bank of Guam which is a US bank incorporated in the territory of Guam. The definitions of “bank” and “banking business” in the Act exempt other financial institutions from the regulatory and supervisory purview of the Board. Both banks have presence in all the four States. Also, both banks are US FDIC insureds, meaning each deposit is insured up to \$250,000. The Bank Act requires that all deposit takers in the FSM must be FDIC insured or equivalent, which is another way of protecting depositor’s interest.

The total number of employees employed by both banks at end 2024 remains at 157. The system realizes a net income (after tax) of \$14.573M compared to \$16.089M in 2023.

#### **Structure of the Board/Commission:**

***The Board or Commission*** is governed by three board members, who are appointed by the President subject to the advice and consent by Congress. The Board is responsible for its own policy. The term for each member is four years; however, the term can be perpetual until a member is replaced. The Banking Commissioner is appointed by the President without term limit, who serves as the CEO and Ex-Officio member of the Board. The staff is employed under the National Government Public Service System, thus subject to the regulations of the Public Service System. Currently, staff includes (1) Bank Examiner, (2) Financial Analyst, and the Secretary/Administrative Officer. The FSM Department of Justice serves as the legal counsel for the Board as provided by the Banking Act. The Board is also permitted under the law to receive other supports from the Government through the President’s Office, such as support from the Public Auditor. By law, the Board is required to meet four times a year. On average, the Board meets seven times a year. Quarterly financials of the banking system required reviewed and submission to the President and the Speaker by the Board, copies are available on our website to whom it may concern. Our website was established to help with the dissemination and publication of reports and other information and activities of the Board that might be of interest to the general public.

***Commissioner*** is responsible for the overall regulatory and supervisory functions which includes, for example, the execution of the Banking Act, any bank related laws, regulations, policies and other prudential banking standards as provided under the law. The Commissioner is responsible for the overall management and implementation of policies, duties and activities of the Board. He is also responsible for ensuring all FDIC imposed requirements are in compliance with by the FDIC insured bank as required

under Article XI of the amended Compact. All bank examination reports are subject to the final approval of the Commissioner.

**Examiner** is primarily responsible for the on-site examinations and overall off-site monitoring analyses and related activities. The Examiner is assisted by the Financial Analyst. As the senior staff, he supervises and overseeing the works of other staff, including but not limited to monthly, quarterly and annual analyses of individual bank and sector-wide financial returns, collection financial sector statistics and information, in-depth and detailed review of bank documents, records, as well as general observations of bank operations. He employs the CAMELS system in assessing and rating performance of the bank which allows for the appropriate levels of supervisory actions and regulatory oversight to ensure the safety, soundness and stability.

**Financial Analyst** is primarily responsible for off-site examination, monitoring and analysis. This involves the collection, review, analysis, and detection of trends and/or singular events that may impact banks' financial condition. This off-site monitoring of financial institutions is conducted monthly, quarterly and as needed in order for monitoring and analysis to take place. This process provides for the opportunity to undertake necessary supervisory action as needed.

**Executive Secretary/Administrative Officer I** is responsible for providing administrative assistance to the entire operation. This includes but not limited to the maintenance of records, documentation processing, preparation monitoring and analysis of budgets, reporting, procurement of supplies and services, tracking and monitoring, among other clerical and related operational and administrative functions.

No new or staff turnover in 2024. However, the Board plans to request for a new Examiner position in its FY26 budget request for there is a need to strengthen the consumer protection compliance side of our operation. In doing so, we hope to bring about specialization into our operation which should result in efficiency and effectiveness.

**Operational Budget** the Board is funded annually through appropriation by the FSM Congress. All fees paid by the banks are deposited in the General Fund. Every January, the Board submits a budget proposal to the President and the Executive Budget Review Committee (EBRC) for consideration and review prior to submission to Congress in April. For fiscal year 2024, Congress appropriated \$270,560 to cover personnel, travel, contractual services, consumable, and fixed assets. There were domestic and international travels, both by Board members and staff. **Annex III** is attached to provide detail information.

**Board Meetings:**

The Board convened six times during the year to deliberate on and dispose of important matters, including quarterly financials, which are published and made available to the general public via our website below.

***Travels:***

There were about thirteen travels during the year, two domestic and eleven international by Board members and staff, some were partially funded by outside sponsors and others fully funded by the appropriation from Congress.

**Major Supervisory Activities of the Board:**

***Anti-Money Laundering (AML) and Counter Financing Terrorism (CFT)***

As stated above, in addition to regular bank regulatory and supervision responsibilities as mandated and stipulated in the Banking Act of 1980, the Board also undertakes and discharges certain functions and oversights pertaining to AML/CFT. This is critical to ensuring safety, stability and soundness of the banking system. For example, in the course of off-site and/or on-site supervision and examination, the Board conducts in-depth and detailed review and analysis of bank documents, records, as well as general observations of bank operations.

The Department of Justice; however, is directly charged with the AML responsibilities under the FSM Codes.

***Off-Site Monitoring:***

As required by law, regulated banks are required to submit periodic financial reports (CALL REPORT) to the Board. Call Report is thoroughly reviewed and analyzed to assess the performances of the banks in terms of compliance with legal standards, conditions of license, strengths, safety and soundness. The analysis forms the basis for the trends and patterns in deposits, loans and other movements and changes in the composition of banks' assets, liabilities and equities. These review and analysis are among the core responsibilities of off-site supervision as outlined in the Strategic Goal No. 2 in its budget. The Bank Financial Analyst compiles, reviews and analyzes the Report prior to further review and analysis by the Banking Examiner before presentation to the Banking Commissioner and the Board.

The data and information reported on the Call Report are compiled into quarterly financial report for presentation to the Board, during which the Board is required to deliberate on such information. If the Board approves, the quarterly financial report is then submitted to the President and Speaker of Congress as required by law. The Report also serves as the basis for policy formulation of the Board. The report is then made available to the general public upon request and also via Board's established website, [www.bankingboard.gov.fm](http://www.bankingboard.gov.fm).

Data submitted by all licensed banks on Call Report or financial prudential returns are entered into a computer database and used in the calculation of pertinent ratios and indicators which help to monitor the performance of individual bank and on a consolidated basis for the banking system. The database is therefore also used for off-site monitoring program and provide comparative analysis and performance tracking for each bank and banking system.

***On-Site Examination:***

The Report received from the Bank serves as an integral part of on-site bank examination planning and scheduling. On-site examinations can either be “spot-examination” or “full-examination”. No on-site bank examination took place in 2024 by the Board. However, the Commissioner and Bank Examiner participated with on-site examinations by FDIC Examination Teams, the financial soundness and consumer compliance examinations.

In addition, the FSM Development Bank (FSMDB) also submits periodic financial statements for compilation and submission to IMF as part of the FSI reporting purpose. FSM Banking Board serves as the focal point for FSI.

***Financial Institutions Not Regulated by the Board:***

As stated above, the Board received expertise advice and opinion from IMF on the need to continue upgrading the legal and regulatory framework for the banking supervision and enhancing the Banking Board’s supervisory capacity to include regulatory and supervisory oversight on the FSM Development Bank and credit unions.

***Issues and Challenges:***

Staff has not been able to attend FDIC Examination School since COVID-19 due to priority given to new FDIC employees and US State Examiners. In other words, priority is given to FDIC staff, State Examiners and FDIC insured banks throughout the US. FDIC School is proven valuable and useful to the staff based on the real and direct relevance to our daily responsibilities. Other trainings are available; however, the fees are quite high and require significant amount of time away from the office.

There are other financial entities, such as, credit unions, money transmitters, third party ATMs and perhaps the FSM Development Bank not currently under regulatory and supervisory purview of the Board. While these entities are not known for accepting “public deposits”, they engage in other financial transactions with the public, and there is a need to ensure public interest is protected. Additionally, data from these institutions is needed if sound decisions for the financial sector are to be made.

Lending in the FSM, if compared to the other Pacific Island countries, is moderate; however, can still be improved. There seems to be some issues inhibiting lending in the FSM, including, for example, lending prime rate is determined by the US Federal Reserves, outmigration, land tenure system, registration and deed, lack of adopted appraisal framework or guideline, lack of credit authority or rating agency, capability of loan applicants to furnish required documents, such as financial statements and receipts, isolation from other markets, among others.

## FINANCIAL CONDITION & PERFORMANCE OF THE COMMERCIAL BANKING SYSTEM

The FSM banking system remained strong and stable in 2024 despite the unprecedented global events, economic policies, and technological advancements that have occurred in the previous years, causing uncertainty in the banking industry worldwide. FSM banks' adaptive capacity in response to evolving economic conditions and their ability to reassess and realign their operational frameworks, investment strategies, and technological infrastructure directly contributes to the stable financial system in 2024.

The banks' financials continue to show improvement during the year as combined *Total Assets* increased by \$29.238 million to \$506.404 million. The composition of total resources of the banking system for the quarter ended December 31, 2024 is broken down as follow:

	US \$ In Thousands	Percentage
Liquid Assets (Cash & Due from Abroad)	\$ 411,832.00	81%
Loan Portfolio	\$ 82,700.00	16%
Bank Premises and Other Assets	\$ 11,872.00	3%
	<b>\$ 506,404.00</b>	<b>100%</b>

**Total Liquid Assets** stood at \$411.832 million and comprised 81% of the system's total assets, an increase over the year by \$30.240 million from \$381.592 million in December 2023. Liquid Assets consist of *Cash* and *Foreign Assets/Due from Banks & Others Abroad*. As of the quarter ended December 31, 2024, *Cash* was at \$5.0 million while *Due from Abroad* was at \$406.9 million.

**Total Loans** slightly declined over the year by \$1.3 million (-1.6%) to \$82.7 million. Commercial lending decreased over the year by \$3.9 million (-8.3%) to \$44.0 million. However, Consumer lending increased over the year by \$2.7 million (7.4%) to \$38.7 million. The loan portfolio comprised 16.0% of the system's total assets, with commercial loans composing 53.3% of the lending portfolio while consumer lending constitutes 46.7%.

On the liabilities & capital side, **Total Deposits** increased over the year by \$28.9 million (6.8%) to \$453.3 million. Total deposits comprised 89.5% of the system's total liabilities and equity. The system's deposit base structure was significantly dominated by Savings deposit facilities at \$232.4 million (51.3%), followed by Demand Deposits at \$180.5 million (39.8%), Time Certificates of Deposits (TCDs) at \$39.9 million (8.8%), with the remaining \$420 thousand (0.1%) for other deposit facilities.

**Total Loan to Deposit** ratio for the system stood at 18.24%. The ratio slightly decreased compared to 19.79% in the same period of 2023.

### Operating Highlights:

- **Total interest income** at year end 2024 was reported at \$24.7 million, an increase from \$24.0 million in the previous year. The **net interest margin** (net interest income/average earning assets) decreased by 18 basis points over the year to 4.85%. The bank reported **prevailing interest rates** on consumer and commercial loans at 14.75% and 4.63% respectively. The **average yield on loans plus invested funds** increased from 5.2% at end-December 2023 to 5.4% at end-December 2024.

- **Total Income** was recorded at \$27.2 million, an increase compared to \$26.3 million in the previous year. **Total Year-to-Date Expenses** (excluding taxes of \$225 thousand) were at \$12.4 million. The banks ended 2024 with \$14.8 million in **Net Operating Income**. The Return on Average Assets (ROAA), net income as a percentage of average assets, declined from 3.34% at end-December 2023 to 3.03% at end-December 2024.
- The **efficiency ratio**, overheads to earnings after deducting interest expense, shows how much each dollar of income is consumed by the banks' operating costs. The efficiency ratio for the system at quarter ended December 31, 2024 showed an improvement over the year as it increased from 32.8% in 2023 to 37.7% in the current year.
- Reported **asset quality** showed slight deterioration during the year as **criticized loans as a percentage of total loans** slightly increased from 7.57% at year-end 2023 to 14.77% at year-end 2024. However, **overdue loans as a percentage of total loans** improved from 2.55% in 2023 to 1.32% in 2024. **Non-accrual loans as a percentage of total loans** also improved from 1.57% in 2023 to 0.67% in 2024. Total **Loan loss reserve** of the banks stood at \$2.5 million as at December 31, 2024, an increase from \$2.4 million in the prior year. The consolidated reserve amount the banks are required to maintain at year end 2024 was \$458 thousand. The amount of loan loss reserve kept by the bank at the end of the year was about 6 times greater than their required reserve amount. The banks reported a year-to-date charge-off of about \$1.2 million, a decrease compared to \$1.8 million in the previous year. Total year-to-date recoveries as at end-December 2024 was \$587 thousand, compared to \$424 thousand in the prior year. Total year-to-date provisions for loan losses were \$710 thousand at end-December 2024 and \$911 thousand in the previous year.
- The banks held **total capital and reserves** at \$40.723 million as of December 31, 2024, an increase by \$1.072 million from \$39.651 million in the same period of 2023.

The banking system's overall performance was assessed as satisfactory as of December 31, 2024, based on the banks' satisfactory levels of capital, earnings, liquidity and strong asset quality indicators as of December 31, 2024.

### ***Capital Adequacy Indicators***

- ❖ **The banks remain well-capitalized.** Total capital and reserves for the system stood at \$40.723 million as of December 31, 2024.
- ❖ The Banking Board monitors each bank to ensure it maintains adequate capital in relation to the size and nature of its business activities. As of December 31, 2024, one bank has maintained capital levels and ratios well above the minimum ratios required by the Banking Board. The other bank operates as a branch in the FSM and currently there is no local capital requirement pursuant to the Bank Act. However, it is stipulated in its Conditions of License issued by the Banking Board that the bank is required to maintain capital, applicable to its global operations, of not less than the capital adequacy requirements directed by the FDIC or the lawful banking supervision authorities in the country of incorporation. Based on the bank's Holding Company

2024 Audited Financial Statements, the bank's aggregate statutory capital exceeded the FDIC's well capitalized standards.

### *Asset Quality Indicators*

- ❖ Asset quality remains satisfactory. Total assets increased over the year by \$29.238 million (6.1%) and the asset base remains high and strong. The increase in total assets over the year was a result of the aggregate \$30.240 million increase in Liquid Assets during the year.
- ❖ Foreign Assets/Due from Banks & Others Abroad comprise 80.3% of the system's Total Assets. Of the \$406.9 million in Liquid Assets invested abroad, \$339.2 million are deposited in demand/overnight and time savings with U.S. FDIC insured banks, \$63.1 million are invested in U.S. Government securities (solely available for sale and guaranteed by the U.S. Government) and \$4.6 million are held in excess balance accounts at the U.S. Federal Reserve. The average yield on these U.S. invested funds at year-end 2024 was 4.41%, an improvement from 4.29% in 2023.
- ❖ **The quality of the system's loan portfolio is satisfactory.** The ratio of Non-Performing Loans to Total Loans stood at 0.67%, improved from 1.57% a year ago. Outstanding Non-Performing Loans improved by 0.90%, or \$766 thousand to \$556 thousand as at year-end 2024. Gross Loans decreased over the year by \$1.3 million (-1.6%); commercial loans decreased over the year by \$3.9 million (-8.3%); however, consumer loans increased by \$2.7 million (7.4%).
- ❖ **Loan Loss Reserves is sufficient.** The current level of loss allowance as of December 31, 2024, is about over five times the level of outstanding Non-Performing Loans for the banking system, indicating that there is sufficient cushioning that well exceeds the potential for loan losses. At December 31, 2024, the level of loss allowance stood at \$2.5 million, well above Banking Board's minimum and recommended level. The banks had reported a year-to-date charge-off of \$1.2 million against recoveries of \$587 thousand.
- ❖ Criticized Loans consist of Substandard, Doubtful and Loss Loans. Loans that fall in these categories are those that either exhibit some weaknesses that jeopardize full repayment of the loans if not promptly corrected, collection or liquidation of the debt in full is highly questionable, or loans become uncollectible or of insufficient current value to warrant being maintained as bankable assets. Substandard loans increased from \$1.5 million in the prior year to \$2.3 million; Doubtful loans also increased over the year from nil to \$2 thousand; and Loss loans reported at nil for both periods. The Banking Board continues to closely monitor and ensure the banks have sound credit risk assessment and measurement process to assess credit risk and account for expected credit losses.

### *Earnings Performance Indicator*

- ❖ **Earnings performance for the banks is satisfactory.** The banks income performance has substantially improved as their aggregated net income has increased to \$14.6 million at year end December 2024.

- ❖ The Banks managed to end year 2024 with \$14.8 million in Net Operating Income owing to the improvement in interest income over the year and the managed levels of interest costs and provisioning for bad loans.
- ❖ The system generated Net Income of \$14.6 million for the period ended December 31, 2024, a decrease compared to \$1.5 million at year-end 2023. Total Interest Income has increased by \$685 thousand to \$24.7 million. Stable profitability is expected for the system and there continues to be potential for further lending growth given sustained excess liquidity.
- ❖ Total Income was recorded at \$27.2 million, an increase from \$26.3 million at year-end 2023. Total interest income improved over the year as yield on invested funds improved from 4.29% in 2023 to 4.41% in 2024.
- ❖ Total Year-To-Date Expenses (excluding taxes of \$225 thousand) was about \$12.4 million, a drop by \$2.4 million from \$10.0 million a year ago.
- ❖ Return on Average Assets/ROAA (net income as a percentage of average assets) has decreased from 3.34% in the prior year to 3.03%—the decrease is proportionate with the decline in net income and slight decrease in average total assets.
- ❖ Net Interest Margin/NIM (net interest income as a percentage of average earning assets) declined over the year to 5.03%, from 4.85% a year ago. The decrease is mainly due to the decline in average yield on invested funds abroad.

### *FSM Banking System*

#### *Consolidated Income and Expense Statement (5 Years)*

(in U.S. '000s)	Dec-20	Dec-21	Dec-22	Dec-23	Dec-24
Interest Income	9,956	8,520	13,444	23,985	24,670
Interest Expense	296	119	314	663	2,264
<b>NET INTEREST INCOME</b>	<b>9,660</b>	<b>8,401</b>	<b>13,130</b>	<b>23,322</b>	<b>22,406</b>
Provisions For Bad Loans Expense	998	330	910	911	710
<b>NON-INTEREST INCOME</b>	<b>1,690</b>	<b>1,801</b>	<b>2,419</b>	<b>2,301</b>	<b>2,494</b>
<b>NON-INTEREST EXPENSE</b>	<b>6,307</b>	<b>6,312</b>	<b>6,736</b>	<b>8,402</b>	<b>9,392</b>
Net Operating Income	4,045	3,560	7,903	16,310	14,798
Less: Taxes	239	291	397	221	225
<b>Net Income</b>	<b>3,806</b>	<b>3,269</b>	<b>7,506</b>	<b>16,089</b>	<b>14,573</b>

#### *Liquidity Indicators*

- ❖ **The banks have high and strong liquidity positions.**
- ❖ Total Liquid Assets stood at \$411.832 million and made up 81.3% of Total Deposits as of December 31, 2024. The ratio increased from 80% in 2023. This means that for every dollar in deposit liabilities, the banking system maintained about 80 cents in liquid assets.



- ❖ Even though local liquid assets (i.e., cash balances) aggregated for both banks cover just 0.98% of Total Liquid Assets, onsite engagements with the banks supplemented with transmitted reports confirmed that both banks maintain sufficient cash and accessible liquidity to meet depositor demands and operational needs.
- ❖ Notwithstanding concerns with the security of their respective liquid assets, banks demonstrate the ability to cover all customer deposits and short-term liabilities and rely more on capital to generate earnings.
- ❖ **All banks in the system demonstrate continued ability to meet depositor demands.**
- ❖ Total Deposits of the system increased over the year by \$28.9 million (6.8%) to \$453.3 million.
- ❖ The ratio of Total Loans to Total Deposits slightly decreased from 19.79% in 2023 to 18.24% in 2024, commensurate with the reported decrease in loans over the year while deposits also decreased. The current ratio means that on average out of every dollar received by the banks, about 20 cents is lent out. This ratio has several implications; including excess deposits continue to be taken in by banks while loans remain stagnant. A couple of challenges remain for FSM inhibiting any significant growth in loans. Namely, lack of legislative support for real estate secured lending and market size (i.e., limited pool of qualified borrowers). Rather than investing locally in terms of expansion in lending activities, the banks continue to place its excess liquidity in US safe and secured interest-earning-assets.

## OTHER BANKING SECTOR STATISTICS

### Financial Access Survey

- ❖ At year-end 2024, there were 30,309 deposit accounts at the commercial banks; of which 2,752 belong to Small Medium Enterprise (SME) accounts and 27,050 belong to household sector accounts. The total number of deposit accounts increased when compared to 28,291 at year end 2023. The increase was due to both increases in household accounts by 1,905 and SMEs by 110. Outstanding deposits at year end 2024 were \$453.3 million; of which \$160 million are in SME accounts and \$104 million are in household accounts. Deposit amounts increased compared to \$424.4 million in 2023. Both banks showed decreases in both the number of accounts and the outstanding deposit amounts during the year.
- ❖ The number of loan accounts at year end 2024 was 7,660; of which 117 belong to SMEs and 6,536 belong to household. Number of loans decreased from 7,877 in 2023. Outstanding loans stood at \$82.7 million; of which \$15.2 million are issued to SMEs and \$37.1 million to households. During the year, the total balance in loans decreased by \$1.3million from \$84.0 million in 2023.

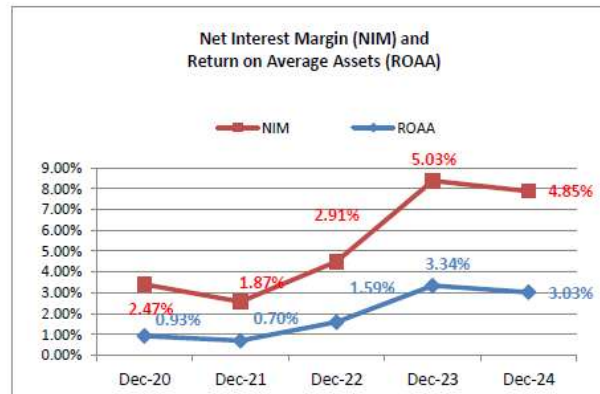
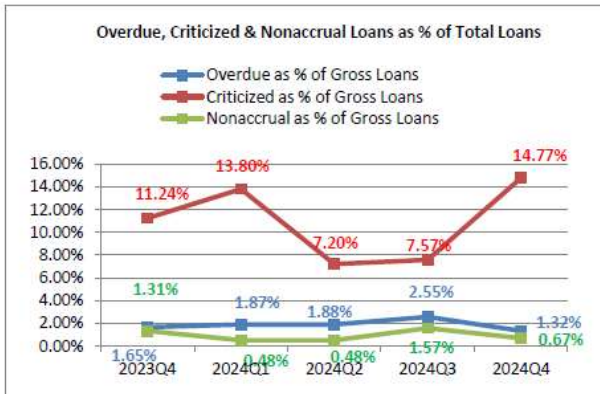
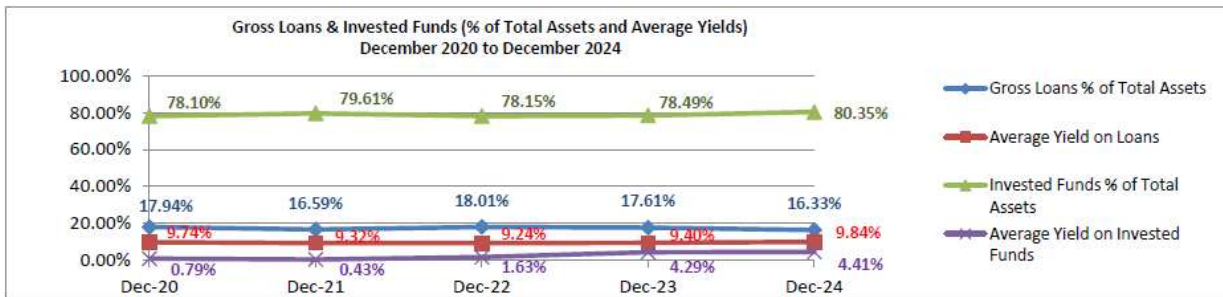
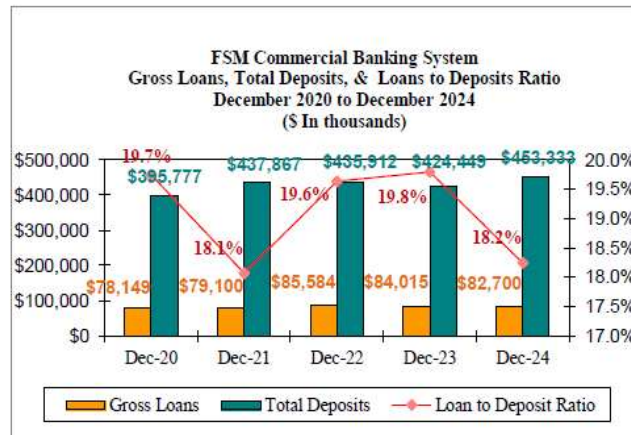
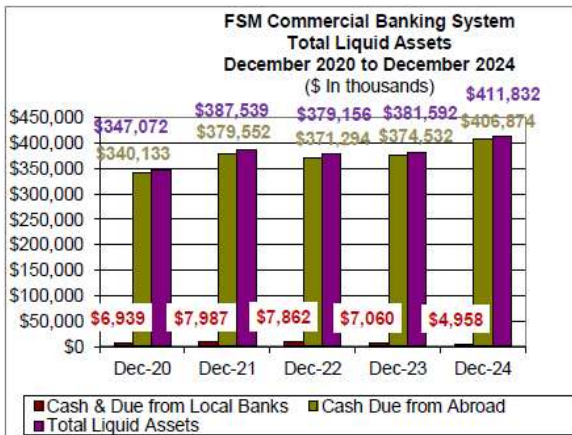
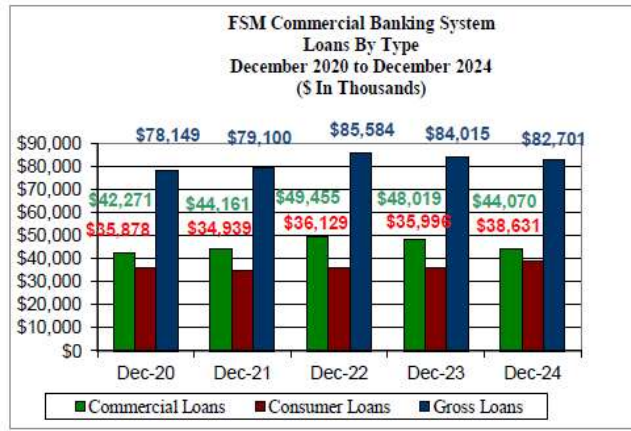
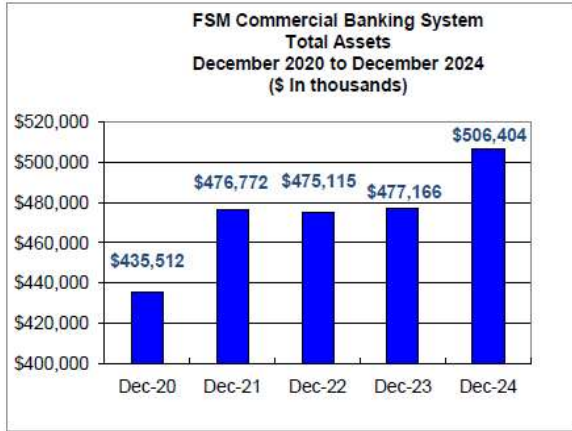
## Key Performance Indicators

KEY RATIOS (%)	December 31, 2023	December 31, 2024
<b>Balance Sheet Ratios:</b>		
Liquid Assets % of Deposits	89.90%	90.85%
Total Loans % of Total Deposits	19.79%	18.24%
Consumer Loans % of Total Loans	42.84%	46.75%
Commercial Loans % of Total Loans	57.16%	53.25%
Invested Funds % of Total Deposits	88.24%	89.75%
Invested Funds % of Total Assets	78.49%	80.35%
Liquid Assets % of Total Assets	79.97%	81.32%
<b>Asset Quality Ratios:</b>		
Overdue Loans as % of Total Loans	2.55%	1.32%
Criticized Loans as % of Total Loans	7.57%	14.77%
Non-Accrual Loans as % of Total Loans	1.57%	0.67%
Loss Reserves as % of Total Loans	2.91%	3.06%
Provisions as % of Total Loans	1.08%	0.97%
Classified as % of Total Loans	7.57%	14.77%
Classified Consumer % of Total Consumer	2.70%	2.26%
Classified Commercial % of Total Commercial	11.21%	25.75%
<b>Interest Measures:</b>		
Average Yield on Loans	9.40%	9.84%
Average Yield on Invested Funds	4.29%	4.41%
Average Cost of Deposits	0.15%	0.52%
Interest Spread (Yield -Cost)	5.07%	4.86%
Net Income to Average Assets (ROAA)	3.34%	3.03%
Net Int Inc to Avg Earning Assets (NIM)	5.03%	4.85%

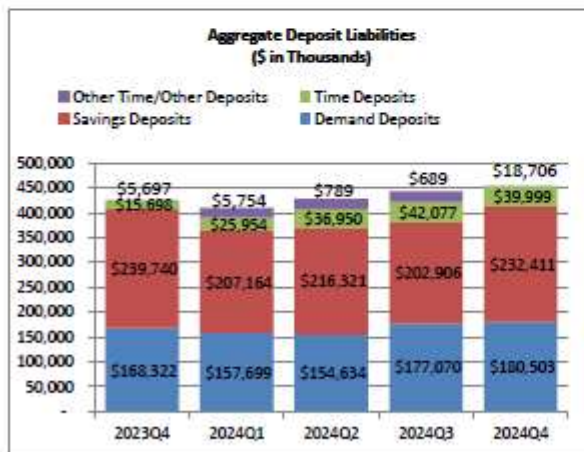
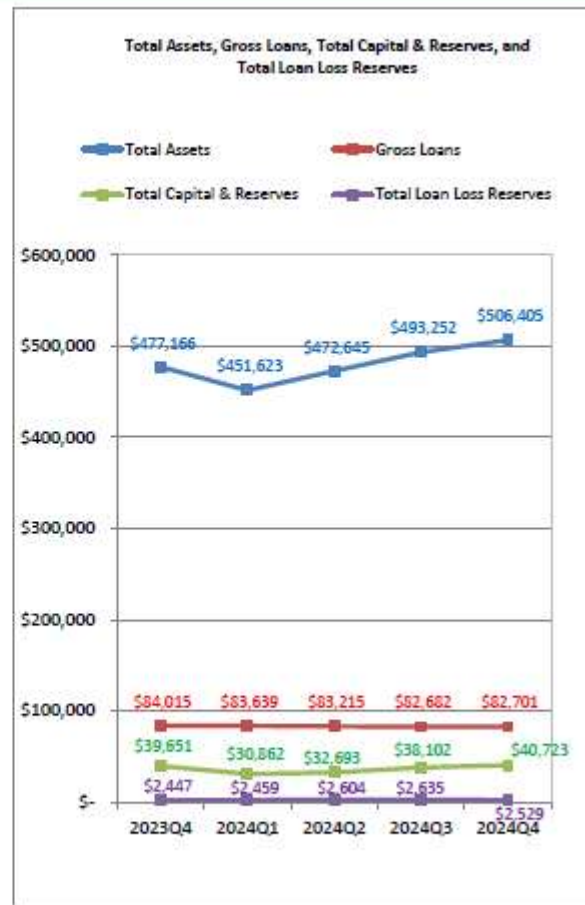
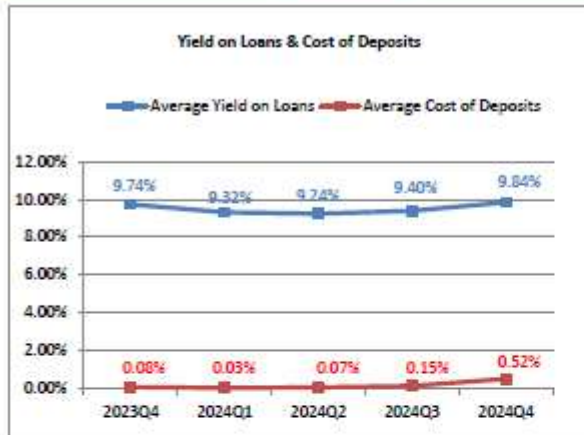
## FINANCIAL SOUNDNESS INDICATORS

<b>Financial Soundness Indicators (Core)</b>	<b>Dec-20</b>	<b>Dec-21</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24</b>
<b>Capital-based</b>					
Regulatory capital to risk-weighted assets	37.57	37.24	38.48	38.95	42.11
Regulatory Tier 1 capital to risk-weighted assets	37.57	37.24	38.48	38.95	42.11
Non-performing loans net of provisions to capital	1.05	2.90	3.72	4.25	6.26
<b>Asset Quality</b>					
Non-performing loans to total gross loans	0.60	1.28	1.43	1.73	2.77
Sectoral distribution of loans to total loans:					
Residents	65.32	68.18	62.64	64.49	63.32
<i>Interbank loans</i>	-	-			
<i>Other financial corporations</i>	-	-			
<i>Non-financial corporations</i>	59.24	62.88	58.45	60.86	60.32
<i>Other domestic sectors</i>	6.07	5.28	4.19	3.63	3.00
Non-residents	34.68	31.84	37.36	35.51	36.68
<b>Earnings and Profitability</b>					
Return on assets	0.91	0.70	1.65	3.37	3.01
Return on equity	13.29	11.71	29.29	46.94	39.20
Interest margin to gross loans	85.12	82.35	84.78	91.02	89.98
Noninterest expense to gross income	57.68	64.72	44.82	33.65	38.62
<b>Liquidity</b>					
Liquid assets to total assets	58.53	67.35	60.74	58.53	60.40
<b>Financial Soundness Indicators (Encouraged)</b>					
Capital to assets	5.59	5.34	5.55	5.81	5.85
Customer deposits to total (non-interbank) loans	506.44	553.56	509.34	505.21	548.16
Personnel expenses to non-interest expenses	51.80	50.16	48.69	45.17	45.26
Foreign -currency-denominated loans to total loans	0.13	0.12	0.12	0.14	0.00

4th Quarter 2024 FSM Commercial Banking System Graphic Reports



4th Quarter 2024 FSM Commercial Banking System Graphic Reports



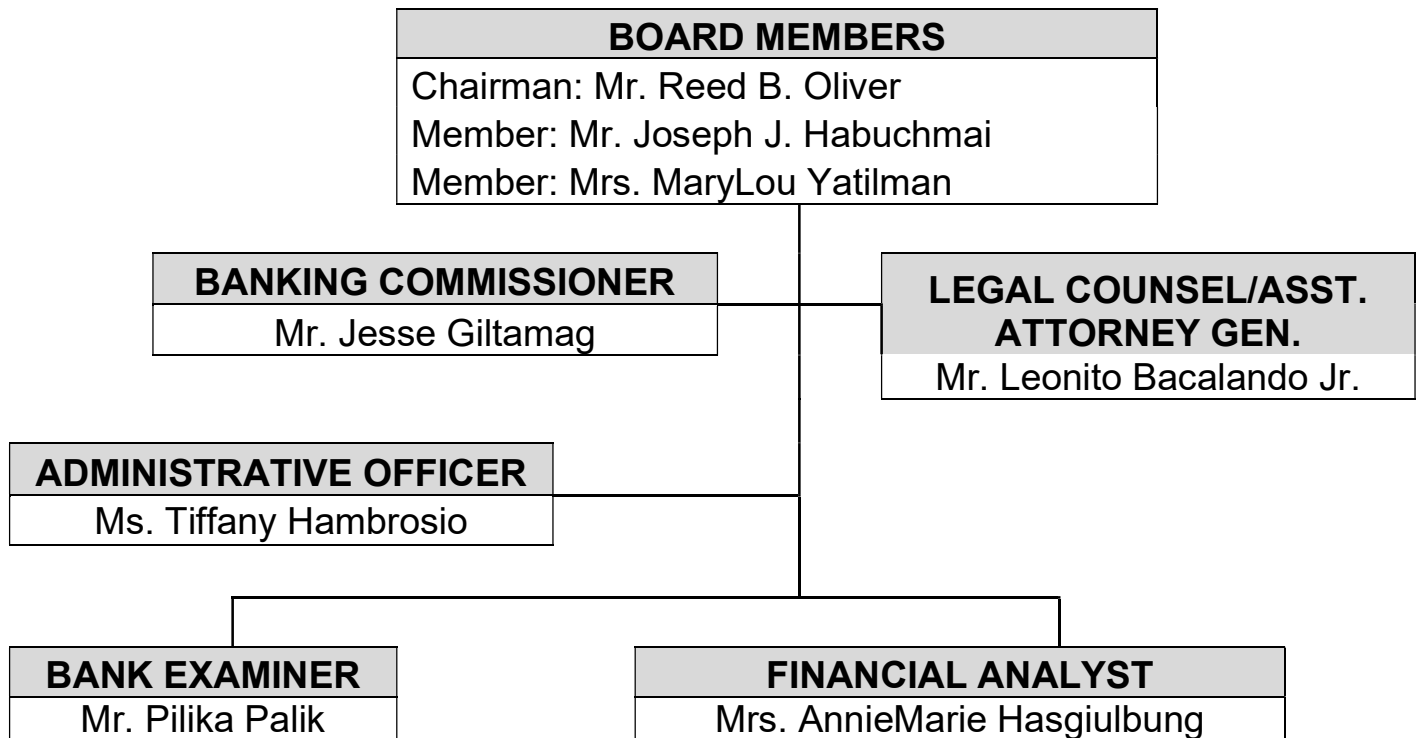
## Annex I: Balance Sheet: December 31, 2024

FSM COMMERCIAL BANKING SYSTEM										
BALANCE SHEET										
December 31, 2024										
	31-Dec-24	%	31-Dec-23	%	Yearly Variance	% Change	30-Sep-24	%	Quarterly Variance	% Change
<b>(US\$ In Thousands)</b>										
<b>ASSETS</b>										
Cash & Due from Local Banks	4,958	1%	7,060	1%	(2,102)	-29.8%	7,339	1%	(2,381)	-32.4%
Foreign Assets/Due from Banks & Others Abroad	406,874	80%	374,532	78%	32,342	8.6%	391,555	79%	15,319	3.9%
<b>Total Liquid Assets</b>	<b>411,832</b>	<b>81%</b>	<b>381,592</b>	<b>80%</b>	<b>30,240</b>	<b>7.9%</b>	<b>398,894</b>	<b>81%</b>	<b>12,938</b>	<b>3.2%</b>
Loans					-				-	
Commercial	44,070	9%	48,019	10%	(3,949)	-8.2%	47,314	10%	(3,244)	-6.9%
Consumer	38,631	8%	35,996	8%	2,635	7.3%	35,368	7%	3,263	9.2%
<b>Total Loans</b>	<b>82,701</b>	<b>16%</b>	<b>84,015</b>	<b>18%</b>	<b>(1,314)</b>	<b>-1.6%</b>	<b>82,682</b>	<b>17%</b>	<b>19</b>	<b>0.0%</b>
Other Assets	11,872	2%	11,559	2%	313	2.7%	11,676	2%	196	1.7%
<b>Total Assets</b>	<b>506,405</b>	<b>100%</b>	<b>477,166</b>	<b>100%</b>	<b>29,239</b>	<b>6.1%</b>	<b>493,252</b>	<b>100%</b>	<b>13,153</b>	<b>2.7%</b>
<b>LIABILITIES &amp; CAPITAL</b>										
Deposits										
Demand	180,503	36%	168,322	35%	12,181	7.2%	177,070	36%	3,433	1.9%
Savings	232,411	46%	239,740	50%	(7,329)	-3.1%	202,906	41%	29,505	14.5%
Time	39,999	8%	15,698	3%	24,301	154.8%	42,077	9%	(2,078)	-4.9%
Other Time/Other Deposits	420	0%	689	0%	(269)	-39.0%	20,674	4%	(20,254)	-98.0%
<b>Total Deposits</b>	<b>453,333</b>	<b>90%</b>	<b>424,449</b>	<b>89%</b>	<b>28,884</b>	<b>6.8%</b>	<b>442,727</b>	<b>90%</b>	<b>10,606</b>	<b>2.4%</b>
Other Liabilities & Capital 1/	53,072	10%	52,717	11%	355	0.7%	50,525	10%	2,547	5.0%
<b>Total Liabilities &amp; Capital</b>	<b>506,405</b>	<b>100%</b>	<b>477,166</b>	<b>100%</b>	<b>29,239</b>	<b>6.1%</b>	<b>493,252</b>	<b>100%</b>	<b>13,153</b>	<b>2.7%</b>
Memorandum Items:										
Loan/Deposit Ratio (%)	18.24%		19.79%				18.68%			
Consumer Loans (% of total loans)	46.71%		42.84%				42.78%			
Commercial Loans (% of total loans)	53.29%		57.16%				57.22%			
Footnote:										
1/ Includes loan loss reserves										
										Source: FSM Banking Board

## Annex II: Organization Chart



### ORGANIZATION OF FSM BANKING BOARD



## Annex III: Fiscal Year 2024 Budget

The total appropriation for Fiscal Year 2024 for the FSM Banking Board was \$270,560, breakdowns on which:

- **Personnel:** \$155,211 was allocated for Personnel and was exhausted out.
- **Travel:** \$50,837 was allocated for travel; left with a surplus of \$24,148.86.
- **Contractual Services:** \$39,402 was allocated for contractual services of which \$20,907.24 was expended.
- **Consumables:** \$25,110 was allocated to consumables. \$2,980.48 was realized as unexpended.
- **Fixed Assets:** \$0

**Chart 1: Appropriated and Expended amount for each Budget Category**

