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Assessing The Impact Of Financial Reporting On Banking Stability: Insights From The 2023 US Banking Sector Turmoil

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ARTICLE INFO	ABSTRACT

The 2023 banking turmoil led to a great inquiry on the financial reporting models and regulations in the US banking system. The US has experienced instances of banking crises, often occasioned by economic downturns. The fall of Silicon Valley Bank, which was the first bank to face closure in 2023, opened up to an address on oversight and regulatory needs of banking institutions. This report highlights the role of financial reporting in the fall of the bank, distinctively categorizing the lack of risk assessments and full disclosure on banking assets as a major reason for the fall of the bank. The report suggests that further disclosures should be made by banks, documenting anticipated risks in their investments and approaches that have to be used to secure and enable sustainable management of unforeseen circumstances. Notably, the banking crisis in 2023, triggered by hikes in interest rates and losses by the banks opened up to more demands for regulatory supervision and protection of customer interests in addressing banking investments.

Keywords— Financial Reporting, Regulation, Financial Statements, Accounting Standards, Banking Regulations

I. Introduction

A. Contextualizing the US 2023 Banking turmoil

In the months between March 2022 and September 2023, the US federal reserve used different financial policies and measures to enhance the status of the economy. The federal reserve increased effective federal funds rate by a high margin of 525 basis points, the highest point of increase since the 1980s. The increased rates affected several banking institutions in the USA, forcing them to adapt their business processes to enable a suitable and appropriate approach to handling the changing times. The action by the federal reserve was however a great step to help in addressing an imminent issue that could have caused an even greater economic tragedy to the community.

Because of these policies, several banks in the US were forced to suffer to the changing times, having been accustomed to long periods of having low interest rates. The high interest rates affected the capacity to operate for major financial institutions in the US [1]. Subsequently, these institutions were forced to face closure, as they lacked in administering and engaging the right advances to achieve some better financial operations.

Difficult times led more than 100 US banks to face losses because of the reduced value of their assets and a difficult economic environment. These banks survived the losses and had to engage different measures to help them in recovering their assets and continually having the right chance to offer their services. However, banks like Silicon Valley bank and Signature Bank faced closure because of the difficult regulations and tough business environment that they had to operate in [2]. Thus, this major issue affected the scope and capacity of banking institutions having to achieve the right consideration in terms of achieving remarkable outcome in their workings.

B. Overview of Financial Reporting in Banking Sector

Financial reporting in US banking institutions demands an approach that necessitates the right step in managing provision of information on their financial activities. The financial reporting in banking sector evaluates their performance on a quarterly or a yearly basis, bringing a tasking influence on the nature of their business operations. The financial reporting role in the banking sector is therefore instrumental in gaining knowledge on operations, economic downturns and approaches that have to be used to sustainably address the growing banking demands amidst economic growth and challenges.

The securities and exchanges commission SEC have a sole mandate of providing regulations on financial reporting in the banking sector. Keen analysis of the banking sector enables a suitable channeling of value to create sustainable modelling of information that is needed from the banks. In the first instance, the SEC works towards establishing key information on the financial reporting documentation [3]. Banks are required to provide information on their financial statements and give inherent risk disclosures on their banking activities. In essence, this model marks the chance to attract and work within the regulatory advancement where banking facilities can work smoothly to obtain the most meaningful and valuable development needed for them.

Financial reporting in banks require reports on capital adequacy. This indicates the banking institutions have to unveil reports on their liquidity and ability to meet business obligations. The capital adequacy remarks a chance to convey their business operations and further growth to enable sustainable engagement with the economy. Banking institutions are therefore mandated to convey about their capitation and further make supplementary disclosures that are related to their course of business in the country [4]. In essence, this implies appropriate modelling to ensure that banks have the right direction in handling their businesses and can provide a profit for the customers.

C. Challenges with Modern Financial Reporting Regulations

Complexity in the regulatory environment is a key challenge affecting the nature and scope of ensuring suitable management of the business needs. The challenges with reporting dictate the several hurdles in catering for the evolving nature of compliance demands in the banking sector. Primarily, the challenge of ensuring similarity in regulatory requirements, accounting standards and effort to have globally harmonized systems affect the reporting for the banking institutions [5]. This challenge stands out as a major influence to the capacity to administer and secure an appropriate level of satisfactory management of banking reporting. Complexity is therefore a key factor that derails an instrumental level of addressing banking needs and even getting to a critical level of addressing growing additions to the financial reporting system.

Financial reporting regulations often require banks to collect, analyze and provide data about their business operations. This challenge affects banking institutions as they have to grapple with more issues relating to data integrity, data quality and privacy regulations that seek to enable a suitable management of their growing concern for the performance. The financial reporting is therefore a tasking action for the institutions, forcing them to adapt to new strategies and models that can sustainably address their growing concerns and needs about sustainable data provisions. Moreover, integrating the disparate systems is a hard factor for the banks, since they have to engage every information that they have to come to a specific standard that contends to the regulatory needs.

Banking businesses are increasingly embracing dynamic business environment and the push for globalization. While these institutions move to secure more assets and engage in several business actions, they face a great shift in reporting and documenting every activity that they have to consider in achieving the required financial reporting. Financial reporting regulations only provide for the conventional banking businesses, leaving a challenge in reporting their ventures and external activities outside the US borders [6]. The challenge affects the financial positioning of the businesses as they have to consistently address the evolving nature of their business when engaging and dealing with consumer reporting guidelines.

II. HISTORICAL CONTEXT OF BANKING CRISES

A. Previous Banking Crises: Causes and Consequences

The financial crisis of 2007-2008 is documented as the most severe economic downturns of the modern times. The financial crisis is often referred to as the great recession was a downturn caused by economic policies and financial approaches by financial institutions, affecting their model of operation. Some of the key causes of the great recession were relaxed lending standards by the financial institutions, a consequence of the credit agencies that assigned high ratings, which did not reflect the actual result of credit scores [7]. The relaxed lending standards, combined with unregulated mortgage lending issues a great distress to banking institutions. Lack of an instrumental regulation guarding lending, mortgage issuance and mortgage-backed securities affected the capacity and scope of registering an imperative result in dealing with the credit card crises. Thus, the banking crisis was caused by a relaxed regulation on lending and provision of mortgages and mortgage-backed securities by banking institutions, affecting their liquidity and capacity to operate in the business market.

The great recession affected the economy in several ways, beginning with the failure of several banking institutions. Banks such as Lehman brothers, Washington Mutual and Bear Stearns faced growing liquidity problems from their high lending rates and several unpaid mortgages that they have given out. The credit crunch also affected the banks, since they could not lend to one another, leading to an even greater crisis, where they did not have the scope and potential to adjust to the remarkable level of appealing to long term business financial requirements [8]. The lack of confidence in the housing market, small businesses and individual lenders soon caused a stock market decline, further making the banks suffer. The consequence of the great recession forced governments to step in and bailout business entities which carried the possibility of continuance despite the growing concern on safety and possibility for fair approaches in sustaining business needs.

B. Role of Financial Reporting in Early Warning Systems

Financial reporting plays an incremental value in informing on the status of a business and mitigations meted by the business to address vulnerabilities. In the banking industry, financial reporting unveils timely information on the financial position, losses, emerging trends and abnormalities within the business. At this stage, the early warning signs can be seen from trend analysis on the performance of the business in the past and present. The use of financial reporting shows abnormal changes in the position of the company, bringing along an instrumental step to achieve sustainable development when handling meaningful and appropriate model of business. Stakeholders and experts can therefore use financial reporting to spot a trend that might affect future liquidity or business performance.

Financial reporting informs stakeholders on the status of disclosure and transparency of the business. Stakeholders such as customers and investors hold a great position in the business, helping them look deeply into any further demands and needs of reporting on their activities. Through disclosures, comparative analysis by stakeholders will help a business highlight the status of performance and it acts as an early warning sign [9]. The scope of providing sustainable information, while working on business projects enables an analysis with similar and competing companies. Therefore, the approach marks a step to look into early warning signs across an industry, or specific to a company, reiterating the demand for more measures and advances in dealing with the growing concern for business growth and adjustments.

Risk management and mitigation models highlight organizational approaches to handle their crises in the financial reports. Reporting about their actions helps to consider the culpability of any situation affecting the company further, or its solution to ensure a critical outcome from the entire approach. Therefore, the risk management and mitigation approaches used by companies help to highlight the essence of a practice or a business venture that the institution has gotten into. Thus, the approach necessitates further inquiry into the possibility of serving as a warning against the business venture [10]. Therefore, the risk management and mitigation approach creates an influential way to consider and look into the further significance of a business, possibility to grow into a bigger crisis and demand for more incentives that will help in achieving better outcomes in the business.

Considerably, financial reporting provides sufficient information on the status of business investments. The reporting documents and unveils key inferences about the business, marking instrumental documentation on the future performance and past influences of the business. Therefore, an appropriate use of the financial reporting marks a key notice on business flaws and possibility to have an integrated solution to avert any crises [11]. Hence, the financial reporting has to be taken up as keen ways to convey information on current and future status of any business activity.

C. Evolution of Regulatory Frameworks in managing banking crises and warning signs

Evolution of regulatory frameworks in handling crises has evolved in the modern era, after every crisis. The evolution is characterized by a need to adapt the financial system and banking institutions to these aspects, leading to an even better scope and level of addressing pertinent issues affecting the banking industry. The adaptations seek to strengthen and empower the financial industry to a level of justifiably ensuring sustainable appeals to handling pertinent crises and upcoming issues in the banking industry.

After the Savings and Loan Crises of the 1980s and 1990s, the financial reporting service unearthed great weaknesses in regulatory frameworks, prompting a further advance to change the phase of the financial sector. The financial reporting therefore changed to introduce risk management practices and enable an oversight on the reporting and provision of information by banking institutions. Subsequently, this reform led to the formation of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 [12].

More to the point, the globalization and financial innovation changes in 1990s to Early 2000s led to a further evolution of the regulatory framework to allow for the changing banking industry. Primarily, the evolution of the banking sector was occasioned with more business activities and opportunities in commercial and investment banking activities. The global growth of the banking industry implied a change to the regulatory framework, giving a chance for the banking institutions to begin investing in more commercial and investment segments that could raise their profits. The advancement of the model to capture innovative businesses and global appeal of banking institutions helped the banks to capture more regulatory modeling to ensure an appropriate integration with policies.

The financial crisis of 2008 revealed underlying financial risks in advancing banking needs to the community. These systemic risks caused the great recession, impacting the scope of determining functionality demands in detailing better and influential steps to achieve remarkable balance in organizational activities. The first evolution was the provision of reforms that sought to help with transparency and disclosure among banking institutions. Risk management regulations also worked to support and adjust to every scope of modelling the crisis, as minimal accountability was experienced in handling risks and achieving a meaningful modelling of the organizational growth to achieve sustainability in all aspects [13]. An evolution into having strict capital requirements was also key to designing a relevant framework to provide caps on business operations that banks had the capacity to get into. Every adjustment to this point meant a better scope and level of considerable growth in terms of achieving safe business environments.

More reforms have since been introduced to banking industry post-2008 financial crisis. Steps to provide supervisory oversight, regulatory compliance and modelling of the businesses to address planning and efficiency have been enacted. The use of resolution planning and stress testing as key approaches to sustainably work within previous challenges offers a strict appeal to management and handling of the financial sector to achieve suitable improvements as needed. Therefore, the reforms have been worked to ensure an integral achievement in resolving financial stress and risks [14]. Framework re-engagement enables banking industry to adapt to the fast-changing environment, looking into key issues such as cybersecurity, climate change and emerging FinTech approaches that disrupt the conventional banking appeals.

III. Theoretical Perspectives on Financial Reporting and Banking Stability

A. Agency Theory and Information Asymmetry

Agency theory discusses corporate governance and financial markets. The theory, alongside the concept of information asymmetry, discloses the level of addressing financial reporting and banking stability in modern times. Agency theory considers the relationship between principals and agents within an organization, addressing decision making and relevant aspects of transparency and disclosure in the company. The theory, alongside information asymmetry, assist in understanding the element of administering a critical step in managing and working for the rightful appeal in enticing organizational advancement to address their reporting needs.

In the banking sector, agency theory considers financial reporting as an instrumental step to help in addressing potential conflict. The agency theory considers functions of both agents and principals, ensuring that financial reporting comes in as a mechanism of addressing the need for constant information about decisions and activities of the company [15]. To this end, managing progressive communication, transparency and openness enables agency theory to provide that there are benefits tied to financial reporting, as all members of the company can consider their position and look at actions that will support collective advancement as desired. The concept of information asymmetry also applies, as understanding the influence of agency theory and financial reporting to sustainably standardize communication, delivery of information on risks, new ventures and capital capacity of the bank.

Agency theory and information asymmetry highlight the benefit of banking stability, detailing the benefits of what every party plays. Working within the framework to ensure alignment to objectives between bank shareholders and executives, it becomes a critical step to understand every key step in administering activities tied to bringing valuable appeal to management needs. Financial reporting helps in advancing the right information to shareholders about pertinent risks through disclosures [16]. An accurate disclosure helps to suitably enhance alignment of the financial institution to shared objectives, creating a distinctive appeal to shareholder interests at all times. Therefore, using agency theory and information asymmetry, an organization has to secure their financial reporting for long term profitability and stability as they have investor confidence and scope of advancing to achieve remarkable progress in their investments.

B. Stakeholder Theory and Accountability

Stakeholder theory details influence of accountability of companies in addressing the needs of both stakeholders and shareholders. Handling the interests of all stakeholders enhances the company's overall accountability for their actions and objectives. This approach sensitizes the demand for accountability in financial reporting of an organization. Stakeholder theory provides an essential step to handling financial reporting, communicating about the company's accountability to report on their activities, having both profits and losses [17]. Thus, the theory provides that stakeholders have to be addressed through financial reporting to get information on disclosures of the company and steps taken to handle every major hurdle they face in the course of the business activities.

Annual and Quarterly filings about the progress and performance of the company provide the chance to equitably work with the demands of the stakeholders. Regular communication on the financial progress and position of the company ascertains stability for banking institutions. With greater stakeholder engagement and communication, more customers get attracted to the company and learn of their services [18]. Essentially, working within this framework places banking institutions at the position where they can grow into innovative businesses and even venture into international business activities. Thus, using stakeholder engagement, regular communication and financial reporting, banks are assured of a stable business framework that involves all parties and communicates of their progress.

C. Institutional Theory and Regulatory Influence

Institutional theory introduces the direct influence of a regulatory environment on organizational operations. The institutional theory highlights the essence of an environment within which corporations function and have to comply to provided restrictions on their operations and activities. When banking institutions work within these regulatory frameworks, they have a greater chance to ensure stability in their actions and achieve the best result in their operations [19]. One of such demands lies within the financial reporting demands, ensuring that banking institutions have the scope and capacity to ensure critical modelling of their activities to ensure critical appeals at all levels. The financial reporting, when rightfully conducted, manages to connect banks to their customers and stakeholders, helping them to conduct their business in the right manner. Hence, the institutional theory provides that sticking to the right regulations, following provided reporting standards and working within the law ensures banks a better step to financial stability in the long run.

IV. CURRENT FINANCIAL REPORTING PRACTICES IN THE BANKING SECTOR

A. Key components of modern Financial Reporting

Modern financial reporting has several components, requiring companies to adhere to every requirement. Primarily, the companies have to provide their financial statements for specific periods and timelines addressing their functionalities. The financial statements include; balance statements, cash flow statements, income statements and statement of changes in equity. These statements help to assess the financial position of the company and their current projects. Additionally, the statements come with notes showing disclosures and clarifications relating to the reports within the specified periods [20]. Within these statements, directors and the organization's management have the task of providing their commentaries and statements about the financial statements of the company at the given period.

Moreover, independent auditor reports are provided within financial statements. Independent auditor reports certify the transparency and accuracy of information captured within the financial statements. Provision of both internal and external audit reports help to justify provided reports in the stated periods. This regulatory provision comes as a key step to achieve sustainable reporting practices within the organization.

Financial reports contain disclosures about pertinent and related organizational activities. Corporate governance disclosures discuss the corporate structure, risk management processes and steps to enable stability in structure and advancement of company's demands. The financial reports help to facilitate and ensure an accurate development of information relating to corporate structure and governance. Sustainability reports such as environmental, social and governance performance models help to convey information of stakeholder interest, promoting the transparency of the company in carrying out their activities [21]. The model creates a suitable step to advance and work within the categorization of major steps to impart value in administering the best business practices, needed for suitable adjustment demands. Therefore, these reports form a key part of financial reporting, as they enhance disclosures on risks, running business investments and opportunities.

B. Regulatory Requirements and Reporting Standards

Banks in USA are subject to regulatory supervision and management through various channels. Different bodies engage in regulatory management and handling of the financial institutions. The federal reserve oversees and regulates banks to ensure they operate sound businesses and it seeks to ensure implementation of monetary policies and devises the framework for operations of these banks. The Federal Deposit Insurance Corporation (FDIC) evaluates safety in banks and insures deposits that are provided within the banking institutions. The regulatory body also resolves any instances of failure within the banking institution to maintain a stable framework where depositors are assured of getting their money, even when the banks fail or go under [22]. The FDIC operates within mainstream financial institutions from banks to credit unions in the country. Another regulatory body is the office of the comptroller of currency (OCC) which supervises adherence to legal provisions and frameworks that enhance banking operations to a level of achieving a satisfactory outcome in addressing their needs. The Consumer Financial Protection Bureau (CFPB) safeguards the consumer interest, ensuring that banking institutions do not engage in unscrupulous dealings that might negatively affect consumers. They regulate the mortgages, credit cards and loans given to individual customers of the businesses.

Regulatory requirements establish a framework for safe operations and management of banking businesses in the US. Capital adequacy and liquidity requirements for the banks establish an instructional step to enable their functionality to achieve the desired goals. The capital requirements enable banks to conduct their operations with ease and absorb losses whenever there are any. The liquidity requirements also enable banks to operate within the short term capacities, enhancing their scope of addressing projections and safeguarding against imminent losses. More to the point, Asset quality and Risk management is a regulatory provision demanding banks to have sound assets that generate revenue and can handle risk management practices aimed at ensuring a secure and instrumental framework of operations for the banking institutions. Finally, banks are required to achieve a level of address to the compliance and anti-money laundering activities. This indicates the banks have the chance to considerably work within legal activities to prevent criminal dealings and enterprises, protecting the general consumer demand for safe banking platforms.

Reporting standards provide that all banks in the USA have to adopt the Generally Accepted Accounting Principles and use it in its reports. The GAAP allows for recording of financial statements and disclosures of the banks, detailing the kind of information available for the banks in the course of their operations. The Financial Accounting Standards Board (FASB) ensures an appropriate management of the GAAP regulations and subsequent applications to the banks [23]. Banks submit these reports, made through consideration of the GAAP framework to their respective regulators, enhancing the timely accountability and transparency about their dealings. Reporting standards and guidelines enable banks to operate in a safe and sound business environment that allows for their growth and profitability.

C. Challenges and Limitations in Financial Reporting

Financial system in US faces several challenges that can affect the scope and potential of enabling appropriate outcomes in all aspects. The main challenges faced by the financial institutions in ensuring appropriate financial reporting are as follows:

a. Complexity in handling Financial Instruments: US banks have to account for several financial instruments such as derivatives, structured projects and securitized projects. This complexity brings a difficulty in addressing the assets that the institutions have, leading to misstatements and errors in financial reporting.
b. Accounting for Off Balance Sheet Activities: Banks indulge in several off-balance business activities that are usually not captured in the traditional business statements. The activities such as contingent liabilities and derivatives trading affect the scope of ensuring successful business need address [24]. Hence, these difficulties reflect in lacking a proper unit of addressing their entire business activities.
c. Regulatory Complexity: Several regulatory bodies, each seeking to ensure compliant banking institutions affects the scope and capacity of ensuring critical handling of the financial statements. It is challenging to address every regulatory body and continue handling business the same way.
d. Cybersecurity and Data Privacy: The constantly evolving threats for banks threaten their functionality and internal controls departments. The banks have to constantly update their security and instill new approaches to help them in safeguarding their business information and secrets.
e. Globalized Business: US banks continually invest in offshore opportunities, calling for the demand to ensure considerable management of their earnings. The complexity of reporting within and outside the US makes it difficult to enable firm financial reporting model across every business entity. Thus, this mechanism affects the scope and capacity of adjusting to individual business needs that will ensure a definitive outcome.

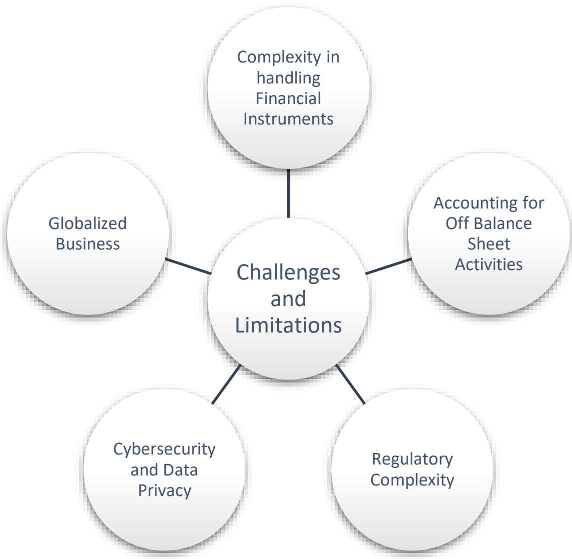

Figure 1: Challenges and Limitations of Financial Reporting

V. Analysis and Review of the 2023 US Banking turmoil

A. Factors Contributing to the Collapse

2023 banking turmoil was a result of interest rate hikes. Massive increases on the interest rates affected banking operations and businesses, leading to negative outcomes in their investments. Most banks in the US invest in government bonds, and the increased rates affected the margin of their earnings [25]. For the longest time, most US banks operated with low interest rates for a long time and continued rise of interest rates from November 2022 to March 2023 implied a long period of losses that hurt their business. Failure to mitigate this risk led to the closure of banks like the Silicon Valley bank and Signature Bank.

B. Role of Financial Reporting Practices in the Collapse of Banks in US

Financial reporting and regulations was a major contributor to the 2023 banking economic downturn. Primarily, the lack of reporting on capital against interest rate risks affected the provision of an instrumental backing against the potential of losses for the banks. The situation with Silicon Valley bank dictated that the banks invested in government bonds, without sufficient risk assessments, leading to their downturn when addressing the requirements of the bank [26]. Essentially, the lack of an appropriate measure on risk management and assessment as well as reporting on banking investments led to a massive fall of the bank once the interest rates hiked.

C. Implication for Banking Regulation and Oversight

2023 banking downturn opened up calls for more regulation and assessment of the banking sector. Demands for greater oversight into the capital against interest rate hikes in banking investments is a key approach taken to enable safety in investments. Moreover, the demand to enable greater stress tests on investments and assessment of individual banking demands creates a suitable approach to facilitate, engage and affirm the right structure in managing banking advances [27]. Therefore, the right modelling and management of the financial sector to handle risks, engage in better management approaches and detail a relevant growth trajectory implies a demand for strict supervision of banking investments and activities.

VI. Lessons Learned and Recommendations

A. Best Practices to be Introduced

Financial reporting on the banking investments have to introduce new dimensions of risk assessment. The risk assessment should cover a wide range of issues that would affect the banking sector and cripple its functionality during occurrences like interest rate hikes. Stronger risk assessments create a meaningful step to ensure adjustment of the economy to ensure an appealing value on the banks [28]. Severity of stress tests on borrower's repayment capacity, occasioned with an even greater demand to restore stability, will ensure banks can function and address their financial progress even in difficult times.

B. Strengthening Regulatory Oversight and Enforcement to assist with stellar banking practices

Regulatory bodies have to engage in stress tests against banks to ensure safety against inflation. Stronger measures on stress associated with banking needs enable a better and more demanding approach to achieve the most meaningful influence over banking activities [29]. The regulatory bodies therefore have to cater for the increasing development of measures to guard against inflation, and fasten their oversight over banking activities and investments, a move to enable sound investments and assets.

C. Enhancing Transparency and Accountability

Financial Reporting in banks has to include every element of their investments. Each asset and investment made by the banks has to show the right framework to assess risks, evaluate their actions and work to a meaningful management of their needs [30]. The financial risks are therefore a major step to understanding the businesses of the banks and structuring outcomes to achieve an even appeal to the customers.

VII. Conclusion

A. Summary of Key Findings

The 2023 banking turmoil resulted into closure of several banks. Key banks like Silicon Valley Bank and Signature Bank closed down because of incapability to continue with business. A major reason for the banking failure was losses caused by interest rate hikes, yet the banks invested a large chunk of their capital on government bonds. The collapse of the banks also led to inquiries on the documentation of capital protection against interest rate hikes and regulation on banking investments. Thus, the federal reserve and regulatory bodies seek to have further restrictions on banking investment and financial reporting about their on and off sheet business activities.

B. Reflection on Importance of Stellar Financial Reporting

The banking turmoil highlights significance of stellar financial reporting that captures banking investments and risk management models. Silicon Valley Bank's lack of appropriate financial reports on the amount of capital investment into government bonds and regulatory risk management models to safeguard contrary outcomes led to a huge loss for the customers. This situation highlights the importance of having a well governed banking management system, where financial reporting caters for every need within the economy.

C. Future Directions and Practice

Financial Reporting should invest in the right measures to secure depositors money and banking investors with early warning signs. Regulators have to work on the right framework to assist in managing banking risks, addressing imminent issues and safeguarding against unprecedented closures. Moreover, further research should be conducted to understand the benefits of banking consolidation and outstanding benefit to the banking industry.

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