Federal Deposit Insurance Corporation
550 17th Street, N.W., Washington, D.C. 20429-9990 Deputy to the Chairman and CFO

May 29, 2019

MEMORANDUM TO: The Board of Directors

FROM: Steven O. App
Deputy to the Chairman
and Chief Financial Officer

SUBJECT: First Quarter 2019 CFO Report to the Board

The attached report highlights the FDIC's financial activities and results for the quarter ended March 31, 2019.

Executive Summary

- During the first quarter of 2019, the Deposit Insurance Fund (DIF) balance rose to $104.9 billion as of March 31, 2019, up $2.3 billion from year-end 2018. The quarterly increase was primarily due to $1.4 billion in assessment revenue and $928 million in interest and unrealized gains on U.S. Treasury securities.

- The reserve ratio, which is the ratio of the DIF balance to estimated insured deposits, was 1.36 percent as of March 31, 2019. The reserve ratio was unchanged from December 31, 2018, as strong seasonal growth in insured deposits offset the growth in the DIF.

- There were no financial institution failures during the first quarter of 2019; the last failure occurred on December 15, 2017.

- Through March 31, 2019, overall FDIC Operating Budget expenditures were below budget by 11 percent ($54.9 million). This variance was primarily the result of vacancies in budgeted positions in the Ongoing Operations budget component and less than expected spending for contractual services in both the Ongoing Operations and Receivership Funding components of the budget.

I. **Financial Results** (See pages 5 – 6 for detailed data and charts.)

Deposit Insurance Fund

- For the first quarter of 2019, the DIF's comprehensive income totaled $2.261 billion, slightly less than comprehensive income of $2.325 billion for the same period last year. The slight decrease of $64 million was primarily the result of a $1.5 billion decrease in assessment revenue (surcharge assessments ended effective October 1, 2018), almost fully offset by a $917 million year-over-year change in unrealized gains/losses on U.S. Treasury securities and a $331 million increase in negative provision for insurance losses.

- The provision for insurance losses was a negative $396 million for the first quarter of 2019, which primarily resulted from a $335 million receipt by one receivership from a litigation settlement related to professional negligence claims. In addition, lower-than-anticipated losses from the early termination of shared-loss agreements contributed $26 million to the negative provision.

Assessments

- During March, the DIF recognized assessment revenue of $1.4 billion, representing the estimate for the first quarter 2019 insurance coverage. Additionally, the DIF recognized a $2 million adjustment for prior period amendments and a $917 thousand adjustment for lower-than-estimated 4th quarter 2018 collections, both of which decreased assessment revenue.

- On March 29, 2019, the FDIC collected $1.4 billion in DIF assessments for fourth quarter 2018 insurance coverage.

II. **Investment Results** (See pages 7 – 8 for detailed data and charts.)

DIF Investment Portfolio

- On March 31, 2019, the total liquidity (also total market value) of the DIF investment portfolio stood at $101.1 billion, up $2.1 billion from its December 31, 2018, balance of $99.0 billion. During the quarter, interest revenue, receivership dividends, and deposit insurance assessment collections far exceeded resolution-related outlays and operating expenses.

- On March 31, 2019, the DIF investment portfolio's yield was 2.11 percent, up 6 basis points from its 2.05 percent yield on December 31, 2018. The new Treasury securities purchased during the quarter generally had higher yields than the maturing securities' yields, some considerably higher.

- In accordance with the approved first quarter 2019 DIF portfolio investment strategy, staff purchased a total of 5 short-maturity conventional Treasury securities, all designated as available-for-sale. The 5 securities had a total par value of $4.5 billion, a weighted average yield of 2.56 percent, and a weighted average maturity of 0.79 years.

III. **Budget Results** (See pages 9 – 10 for detailed data.)

Approved Budget Modifications

The 2019 Budget Resolution delegated to the Chief Financial Officer (CFO) and selected other officials the authority to make certain modifications to the 2019 FDIC Operating Budget. The following budget reallocations were approved during the first quarter in accordance with the authority delegated by the Board of Directors.

- In January, the Chief Information Officer (CIO) Council, Corporate University, the Legal Division, the Division of Information Technology (DIT), and the Office of Chief Information Security Officer (OCISO) reallocated budget authority among major expense categories within their Ongoing Operations budgets.

- In March, following establishment of the FDiTech Lab, the CFO approved the reallocation of $792,752 from the Corporate Unassigned contingency reserve to create an initial 2019 Ongoing Operations budget for the new organization. The initial budget consists of $760,052 for Salaries and Compensation, $30,000 for Travel, and $2,700 for Other Expenses. This change was not reflected in budget totals until April.

Following these first quarter budget modifications (including the FDiTech Lab budget implemented in April), the balances in the Corporate Unassigned contingency reserves were $11,707,248 in the Ongoing Operations budget component and $8,994,445 in the Receivership Funding budget component.

Approved Staffing Modifications

The 2019 Budget Resolution delegated to the CFO the authority to modify approved 2019 staffing authorizations for divisions and offices, as long as those modifications did not increase the total approved 2019 FDIC Operating Budget.

- In March, the CFO approved a decrease of four authorized permanent Supervisory Examiner (SE) positions (revised in April to a decrease of five authorized permanent SE positions) and an increase of one authorized non-permanent SE position in RMS's 2019 staffing authorization, based on an updated analysis of field office supervisory spans of control.

Also in March, the CFO approved an initial 2019 staffing authorization of two new authorized permanent positions for the FDiTech Lab. The new organization will be staffed this year primarily through the temporary detail of FDIC employees to the FDiTech Lab to work on specific projects.

Spending Variances

Significant spending variances by major expense category and division/office are discussed below. Significant spending variances for the three months ending March 31, 2019, are defined as those that either (1) exceed the YTD budget by more than $3 million and represent more than five percent of a major expense category or total division/office budget; or (2) are under the YTD budget for a major expense category or division/office by an amount that exceeds $15 million and represents more than fifteen percent of the major expense category or total division/office budget.

Significant Spending Variances by Major Expense Category

<u>Ongoing Operations</u>

There was a significant spending variance during the first quarter in one major expense category of the Ongoing Operations budget component.

Spending in the Equipment major expense category exceeded the YTD budget by $3.1 million, or 13 percent. The organizations reporting to the CIO (DIT, CIO Council, and OCISO) accounted for most of the variance, with a combined overspending of $2.7 million, or 21 percent of their total YTD budgets for Equipment. This variance was attributable principally to the delayed acquisition of security equipment for the Backup Data Center ($876,525 for purchases that were originally expected to occur in 2018), erroneous coding to the Equipment category ($800,823) and an unbudgeted subscription charge ($993,000). The accounting errors were caused by two year-end accruals that were incorrectly coded to the Equipment expense category (these errors have now been corrected).

Receivership Funding

The Receivership Funding component of the 2019 FDIC Operating Budget includes funding for expenses that are incurred in conjunction with institution failures and the management and disposition of the assets and liabilities of the ensuing receiverships, except for salary and benefits expenses for permanent employees assigned to the receivership management function and other expenses required to ensure readiness without regard to whether failures occur.

There was a significant spending variance during the first quarter in one major expense category of the Receivership Funding budget component.

Outside Services – Personnel expenses during the first quarter were $17.4 million, or 47 percent, less than budgeted. This variance was mostly attributable to under-spending by the Division of Resolutions and Receiverships (DRR) of $11.1 million, or 51 percent, of its YTD budget for contractual support for pre-closing, closing, and post-closing receivership operations; accounting services; asset marketing and management; and resolutions-related activities. This was largely attributable to the fact that there were no bank closings in the first quarter. In addition, the Legal Division spent $6.1 million, or 43 percent, less than budgeted because it did not accrue for unpaid invoices for outside counsel expenses.

Office of Inspector General

There were no significant spending variances during the first quarter in any major expense category of the Office of the Inspector General budget component.

Significant Spending Variances by Division/Office[1]

One organization had a significant spending variance through the end of the first quarter.

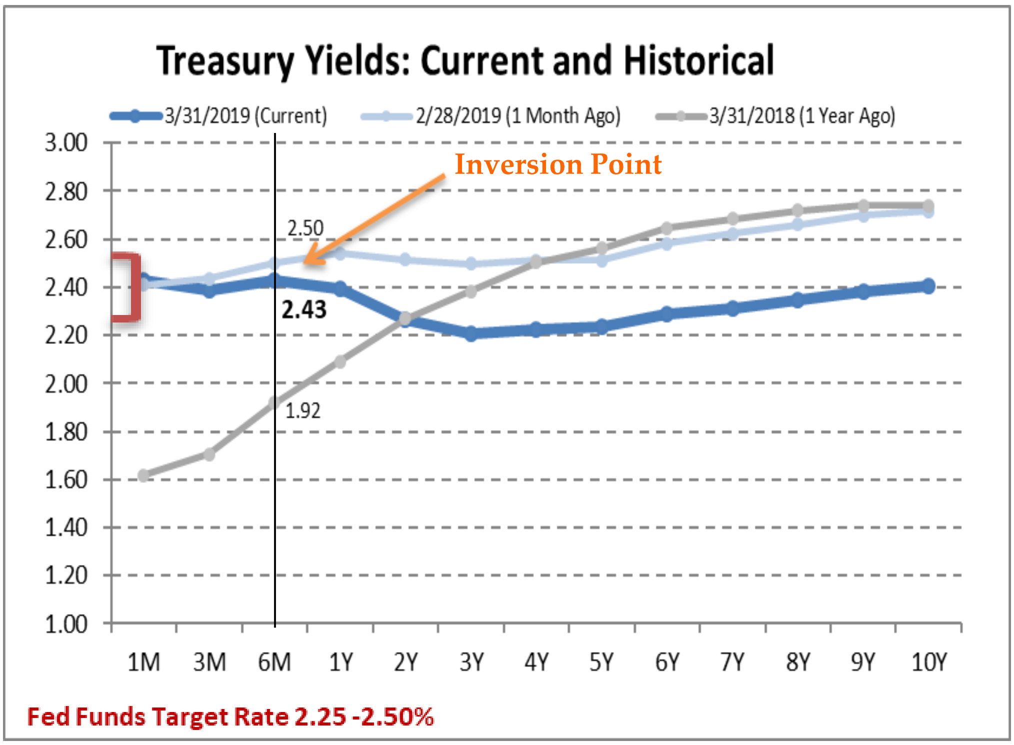
DRR spent $15.3 million, or 29 percent, less than budgeted due to the lack of closing activity in the first quarter and a one-time credit of $317,000 for an insurance payment for hurricane damage to owned real estate.

[1] Information on division/office variances reflects variances in the FDIC Operating Budget.

Fund Financial Results

($ in Millions)

Balance Sheet	Deposit Insurance Fund				
			Quarterly		Year-Over-Year
	Mar-19	Dec-18	Change	Mar-18	Change
Cash and cash equivalents	$ 7,062	$ 5,774	$ 1,288	$ 3,119	$ 3,943
Investment in U.S. Treasury securities	93,507	92,708	799	84,831	8,676
Assessments receivable	1,372	1,376	(4)	2,783	(1,411)
Interest receivable on investments and other assets, net	567	550	17	581	(14)
Receivables from resolutions, net	3,187	3,058	129	5,194	(2,007)
Property and equipment, net	324	329	(5)	325	(1)
Total Assets	$ 106,019	$ 103,795	$ 2,224	$ 96,833	$ 9,186
Accounts payable and other liabilities	211	198	13	200	11
Liabilities due to resolutions	554	605	(51)	1,154	(600)
Postretirement benefit liability	236	236	(0)	259	(23)
Contingent liability for anticipated failures	115	114	1	113	2
Contingent liability for guarantee payments and litigation losses	33	33	(0)	35	(2)
Total Liabilities	$ 1,149	$ 1,186	$ (37)	$ 1,761	$ (612)
FYI: Unrealized gain (loss) on U.S. Treasury securities, net	(194)	(615)	421	(975)	781
FYI: Unrealized postretirement benefit (loss) gain	(14)	(14)	0	(46)	32
Fund Balance	$ 104,870	$ 102,609	$ 2,261	$ 95,072	$ 9,798



The Treasury yield curve is now inverted reflecting concerns about economic growth both in the U.S. and internationally. The short end of the curve is anchored due to the current Fed Funds Target which is set to 2.25-2.50%. The inversion which starts in the 6-month sector became stronger in February and reflects growing concerns for a mild recession in 2020 and market speculation that there will be no Fed rate hikes and even the possibility of a cut in the next year. At the same time, inflation remains muted which is keeping yields for the longer maturity sectors down and fairly flat.

Fund Financial Results - continued

($ in Millions)

Income Statement (year-to-date)	Deposit Insurance Fund			
	Mar-19	Dec-18	Mar-18	Year-Over-Year Change
Assessments	$ 1,369	$ 9,527	$ 2,850	$ (1,481)
Interest on U.S. Treasury securities	507	1,633	338	169
Other revenue	2	11	1	1
Total Revenue	$ 1,878	$ 11,171	$ 3,189	$ (1,311)
Operating expenses	434	1,765	433	1
Provision for insurance losses	(396)	(563)	(65)	(331)
Insurance and other expenses	0	3	0	0
Total Expenses and Losses	$ 38	$ 1,205	$ 368	$ (330)
Net Income	1,840	9,966	2,821	(981)
Unrealized gain (loss) on U.S. Treasury securities, net	421	(136)	(496)	917
Unrealized postretirement benefit gain (loss)	0	32	0	0
Comprehensive Income	$ 2,261	$ 9,862	$ 2,325	$ (64)

Selected Financial Data	FSLIC Resolution Fund				
	Mar-19	Dec-18	Quarterly Change	Mar-18	Year-Over-Year Change
Cash and cash equivalents	$ 907	$ 902	$ 5	$ 889	$ 18
Accumulated deficit	(124,582)	(124,587)	5	(124,601)	19
Total resolution equity	908	902	6	889	19
Total revenue	5	17		3	2
Operating expenses	0	0		0	0
Losses related to thrift resolutions	0	0		0	0
Net Income (Loss)	$ 5	$ 17		$ 3	$ 2

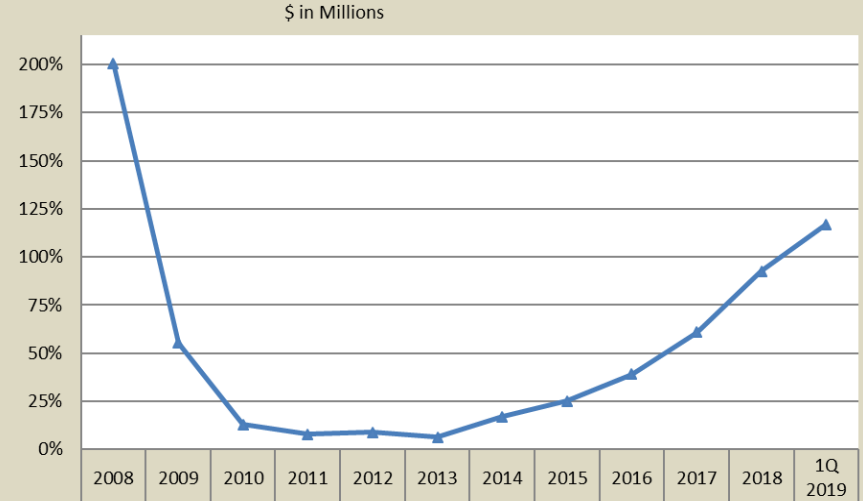
Receivership Selected Statistics March 2019 vs. March 2018

	DIF			FRF			ALL FUNDS		
($ in millions)	Mar-19	Mar-18	*Change*	Mar-19	Mar-18	*Change*	Mar-19	Mar-18	*Change*
Total Receiverships	271	317	(46)	0	0	0	271	317	(46)
Assets in Liquidation	$ 1,035	$ 2,097	$ (1,062)	$ 2	$ 2	$ 0	$ 1,037	$ 2,099	$ (1,062)
YTD Collections	$ 400	$ 492	$ (92)	$ 0	$ 0	$ 0	$ 400	$ 492	$ (92)
YTD Dividend/Other Pmts -	$ 255	$ 847	$ (592)	$ 0	$ 0	$ 0	$ 255	$ 847	$ (592)

Coverage Ratio

Interest on U.S. Treasury (UST) Securities as a percentage of Operating Expenses

$ in Millions



	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	1Q 2019
Coverage Ratio	201%	55%	13%	8%	9%	6%	17%	25%	39%	61%	93%	117%
Interest on UST securities	2,072	704	205	128	159	103	282	423	671	1,057	1,633	507
Operating Expenses	1,033	1,271	1,593	1,625	1,778	1,609	1,664	1,687	1,715	1,739	1,765	434

Since 2013, the coverage ratio has steadily risen as a result of significant increases in interest revenue on U.S. Treasury securities, nominally offset by increases in operating expenses.

Increases in interest revenue on U.S. Treasury securities are due to: 1) increases in the federal funds target rate, 2) higher yields on new long-term investments purchased as older long-term investments matured, and 3) steady growth in the investment portfolio balance.

Deposit Insurance Fund Portfolio Summary

(Dollar Values in Millions)

	3/31/19	12/31/18	Change
Par Value	$101,105	$99,339	$1,766
Amortized Cost	$100,856	$99,063	$1,793
Total Market Value (including accrued interest)	$101,079	$98,954	$2,125
Primary Reserve [1]	$101,079	$98,954	$2,125
Primary Reserve % of Total Portfolio	100.0%	100.0%	0.0%
Yield-to-Maturity [2]	2.11%	2.05%	0.06%
Weighted Average Maturity (in years)	1.53	1.75	-0.22
Effective Duration (in years)			
Total Portfolio	1.48	1.69	-0.21
Available-for-Sale Securities	1.61	1.79	-0.18
Held-to-Maturity Securities [3]	not applicable	not applicable	not applicable

[1] Primary Reserve is the total market value (including accrued interest) of overnight investments, all available-for-sale securities (AFS), and held-to-maturity (HTM) securities maturing within three months.

[2] The Yield-to-Maturity includes the potential yields of any Treasury Inflation-Protected Securities (TIPS), which assumes an average 2.0% annual increase in the CPI over the remaining life of each TIPS.

[3] In early August 2008, management reclassified all of the DIF portfolio's HTM securities as AFS securities effective as of June 30, 2008, because the FDIC could no longer assert it had the positive intent and ability to hold its HTM securities until their maturity dates.

Summary of Other Corporate Investment Portfolios

(Dollar Values in Millions)

	3/31/19	12/31/18	Change
FRF-FSLIC			
Book Value [4]	$862	$857	$5
Yield-to-Maturity	2.47%	2.42%	0.05%
Weighted Average Maturity	overnight	overnight	no change

[4] Due to the current short-term nature of this portfolio, its respective Par, Book, and Market Values are identical for reporting purposes.

National Liquidation Fund (NLF) Investment Portfolio Summary

(Dollar Values in Millions)

	3/31/19	12/31/18	Change
Book Value [5]	$3,079	$2,988	$91
Effective Annual Yield	2.50%	2.46%	0.04%
Weighted Average Maturity (in days)	37	51	(14)

[5] Due to the short-term nature of the NLF portfolio, its Book and Market Values are identical for reporting purposes.

Investment Strategies	
DEPOSIT INSURANCE FUND	**Strategy for the 1st Quarter 2019** Purchase up to \$12 billion (par value) of Treasury securities with maturity dates between June 30, 2019, and December 31, 2023, subject to the following additional provisions: all newly purchased securities will be designated as AFS; no more than \$2 billion (adjusted par value) of such securities shall consist of TIPS; and no "soft target" minimum investment for newly purchased Treasury securities in the 3- to 5-year maturity sectors.
	Strategy Changes for the 2nd Quarter 2019
	Purchase up to <u>\$15 billion</u> (par value) of Treasury securities with maturity dates between <u>September 30, 2019</u>, and December 31, 2023, subject to the following additional provisions: all newly purchased securities will be designated as AFS; no more than \$2 billion (adjusted par value) of such securities shall consist of TIPS; and no "soft target" minimum investment for newly purchased Treasury securities in the 3- to 5- year maturity sectors.
NATIONAL LIQUIDATION FUND	**Strategy for the 1st Quarter 2019** Maintain an overnight deposit target floor balance within a range of \$100 million to \$300 million. Strategically invest the remaining funds in the zero- to 12-month maturity sector.
	Strategy Changes for the 2nd Quarter 2019
	No strategy changes for the second quarter of 2019.

Executive Summary of 2019 Budget and Expenditures
by Budget Component and Major Expense Category
Through March 31, 2019
(Dollars in Thousands)

Major Expense Category	Annual Budget	YTD Budget	YTD Expenditures	% of YTD Budget Used	YTD Variance
FDIC Operating Budget					
Ongoing Operations					
Salaries & Compensation	$1,238,631	$315,479	$292,643	93%	($22,836)
Outside Services - Personnel	257,631	59,255	51,663	87%	(7,591)
Travel	85,014	20,924	17,593	84%	(3,331)
Buildings	107,516	24,968	23,501	94%	(1,467)
Equipment	107,853	24,628	27,715	113%	3,087
Outside Services - Other	15,991	3,607	3,109	86%	(498)
Other Expenses	12,828	3,828	3,233	84%	(595)
Total Ongoing Operations	**$1,825,464**	**$452,689**	**$419,457**	**93%**	**(33,232)**
Receivership Funding					
Salaries & Compensation	$3,804	$1,237	$788	64%	($449)
Outside Services - Personnel	156,634	36,791	19,440	53%	(17,351)
Travel	3,272	816	272	33%	(544)
Buildings	5,488	1,371	298	22%	(1,073)
Equipment	1,160	290	110	38%	(180)
Outside Services - Other	1,023	255	345	135%	90
Other Expenses	3,619	903	68	8%	(835)
Total Receivership Funding	**$175,000**	**$41,663**	**$21,321**	**51%**	**($20,342)**
Office of Inspector General					
Salaries & Compensation	$37,013	$9,253	$8,030	87%	($1,223)
Outside Services - Personnel	1,595	399	744	186%	345
Travel	1,218	304	307	101%	3
Buildings	0	0	0		0
Equipment	2,686	672	347	52%	(325)
Outside Services - Other	0	0	0		0
Other Expenses	470	118	39	33%	(79)
Total Office of Inspector General	**$42,982**	**$10,746**	**$9,467**	**88%**	**($1,279)**
Total FDIC Operating Budget	**$2,043,446**	**$505,098**	**$450,245**	**89%**	**($54,853)**

Executive Summary of 2019 Budget and Expenditures by Division/Office Through March 31, 2019 (Dollars in Thousands)					
Division/Office	Annual Budget	YTD Budget	YTD Expenditures	% of YTD Budget Used	YTD Variance
FDIC Operating Budget					
Risk Management Supervision	$581,235	$148,608	$136,497	92%	($12,111)
Resolutions & Receiverships	208,689	52,967	37,706	71%	(15,261)
Administration	269,286	71,518	65,693	92%	(5,825)
Legal	192,595	48,801	39,172	80%	(9,629)
Information Technology	245,953	53,300	50,351	94%	(2,949)
Depositor & Consumer Protection	180,935	46,410	42,938	93%	(3,472)
Insurance & Research	56,302	14,039	13,051	93%	(988)
CIO Council	50,970	12,239	13,531	111%	1,292
Finance	43,127	10,815	9,620	89%	(1,195)
Inspector General	42,982	10,746	9,467	88%	(1,279)
Chief Information Security Officer	51,036	11,615	9,979	86%	(1,636)
Executive Support [1]	22,828	5,439	4,642	85%	(797)
Complex Financial Institutions	20,985	5,062	4,499	89%	(563)
Corporate University - Corporate	22,590	5,827	6,371	109%	544
Corporate University - CEP	19,364	4,548	3,934	86%	(614)
Executive Offices [2]	13,075	3,164	2,794	88%	(370)
Corporate Unassigned [3]	21,494	0	0		0
Total FDIC Operating Budget	**$2,043,446**	**$505,098**	**$450,245**	**89%**	**($54,853)**

1) Executive Support includes the Offices of Minority and Women Inclusion, Communications, Ombudsman, Legislative Affairs, and Financial Institution Adjudication.

2) Executive Offices include the offices of the Chairman, Vice Chairman, Independent Director, Deputy to the Chairman and Chief Operating Officer, Deputy to the Chairman and Chief Financial Officer, and Chief Information Officer.

3) Does not include reallocation of $792,752 for FDiTech Lab, approved in March, but due to coding requirements not reflected until April.