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

May 16, 2018

MEMORANDUM TO: The Board of Directors

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

Craig R. Jarvill
Director, Division of Finance

SUBJECT: First Quarter 2018 CFO Report to the Board

The attached report highlights the FDIC's financial activities and results for the quarter ended March 31, 2018.

Executive Summary

- During the first quarter of 2018, the Deposit Insurance Fund (DIF) balance was $95.1 billion, up $2.3 billion from year-end 2017. The quarterly increase was primarily due to $2.9 billion of assessment revenue, partially offset by a $496 million unrealized loss on U.S. Treasury securities.

- The reserve ratio, which is the ratio of the DIF balance to estimated insured deposits, was 1.30 percent for first quarter 2018, unchanged from fourth quarter 2017, due primarily to strong growth in estimated insured deposits.

- There were no financial institution failures during the first quarter of 2018.

- Through March 31, 2018, overall FDIC Operating Budget expenditures were below budget by 7 percent ($35 million). This variance was primarily the result of vacancies in budgeted positions and less than expected contractual services in both the Ongoing Operations and Receivership Funding components of the budget.

I. <u>Financial Results</u> (See pages 5 – 6 for detailed data and charts.)

Deposit Insurance Fund

- For the first quarter of 2018, the DIF's comprehensive income totaled $2.3 billion, compared to comprehensive income of $1.8 billion for the same period last year. This $559 million increase was primarily the result of an $830 million decrease in provision for insurance losses and a $113 million increase in assessment revenue, partially offset by a $503 million reduction to comprehensive income from unrealized losses on U.S. Treasury securities (year-to-date 2018 unrealized loss of $496 million versus year-to-date 2017 unrealized gain of $7 million).

- The provision for insurance losses was a negative $65 million for the first quarter of 2018, compared to a positive $765 million for the same period last year. The 2017 provision was primarily attributable to an increase in estimated losses for anticipated failures.

- During the first quarter 2018, DIF incurred a $496 million unrealized loss on its portfolio of U.S. Treasury securities as a result of yields rising dramatically across all maturity sectors of the Treasury yield curve. This rise resulted in declines in the securities' market values relative to their book values.

Assessments

- During March, the DIF recognized assessment revenue of $2.9 billion. Of this amount, $1.5 billion represented the estimate for the first quarter 2018 insurance coverage and $1.3 billion represented estimated assessment surcharges on banks with $10 billion or more in assets. Additionally, the DIF recognized a $100 million adjustment for higher-than-estimated collections for the fourth quarter 2017 insurance coverage (regular assessments: $91 million and surcharges: $9 million), which increased assessment revenue. This adjustment was primarily due to higher-than-estimated assessment rates for many large banks.

- On March 30, 2018, the FDIC collected $1.5 billion in DIF regular assessments and $1.3 billion in surcharge assessments for fourth quarter 2017 insurance coverage.

II. <u>Investment Results</u> (See pages 7 – 8 for detailed data and charts.)

DIF Investment Portfolio

- On March 31, 2018, the total liquidity (also total market value) of the DIF investment portfolio stood at $88.5 billion, up $2.9 billion from its December 31, 2017, balance of $85.6 billion. During the quarter, interest revenue, receivership dividends, and deposit insurance assessment collections far exceeded resolution-related outlays and operating expenses.

- On March 31, 2018, the DIF investment portfolio's yield was 1.63 percent, up 11 basis points from its 1.52 percent yield on December 31, 2017. 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 2018 DIF portfolio investment strategy, staff purchased a total of 23 short- to intermediate-maturity conventional Treasury securities, all designated as available-for-sale. The 23 securities had a total par value of $7.7 billion, a weighted average yield of 2.23 percent, and a weighted average maturity of 2.78 years.

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

Approved Budget Modifications

The 2018 Budget Resolution delegated to the Chief Financial Officer (CFO) and selected other officials the authority to make certain modifications to the 2018 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 2018, several divisions and offices reallocated funds among expense categories within their approved budgets to better align their budgets with updated projections of spending by expense category for the year. Most of these administrative realignments involved very small amounts.

  - Corporate University made the largest realignment in the Ongoing Operations budget component, transferring almost $600,000 from the Outside Services – Personnel expense category to the Equipment expense category. This reallocation was made to properly account for projected spending for on-line information services and IT licenses that had previously been treated as contracts.

  - The largest realignment in the Receivership Funding budget component was made by the Division of Resolutions and Receiverships, which reallocated approximately $1 million from the Travel expense category to the Other Expenses category to provide budget resources for anticipated costs associated with tax return preparation.

- In February 2018, the CFO approved the reallocation of $510,000 within the Ongoing Operations budget component from the Corporate Unassigned contingency reserve to the Division of Information Technology's (DIT) Outside Services – Personnel budget. These additional funds will be used by DIT for one-time costs associated with the migration of Office of Inspector General (OIG) e-mail to a separate Office 365 online environment.

- In March 2018, the CFO approved the reallocation of $525,164 within the Ongoing Operations budget component from the Corporate Unassigned contingency reserve to various budgets within the Executive Offices. These funds will ensure adequate resources are available to support updated expense projections for the year. Funds were adjusted in the Salaries and Compensation and Travel expense categories of several individual offices.

Following these first quarter budget modifications, the balances in the Corporate Unassigned contingency reserves were $23,964,836 in the Ongoing Operations budget component and $23,850,871 in the Receivership Funding budget component.

Approved Staffing Modifications

The 2018 Budget Resolution delegated to the CFO the authority to modify approved 2018 staffing authorizations for divisions and offices, as long as those modifications did not increase the total approved 2018 FDIC Operating Budget.

- In February, the CFO approved the following staffing modifications:

  - After a review of authorized and on-board staffing levels in the Office of Minority and Women Inclusion (OMWI) and an assessment of OMWI's anticipated workload, the CFO approved the Acting OMWI Director's request to reduce OMWI's 2018 permanent staffing allocation by one position.

- One authorized permanent position was realigned from the CFO's office to the Division of Administration (DOA) to support DOA's internal review and risk management program.

- In March, the CFO approved an increase of one position in RMS's 2018 staffing authorization to address a requirement for one additional Supervisory Examiner positon, based on an updated analysis of field office supervisory spans of control.

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, 2018, 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 were no significant spending variances during the first quarter in any major expense category of the Ongoing Operations budget component of the 2018 FDIC Operating Budget.

<u>Receivership Funding</u>

The Receivership Funding component of the 2018 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.

There were no significant spending variances during the first quarter in any major expense category of the Receivership Funding budget component of the 2018 FDIC Operating Budget.

<u>Office of Inspector General</u>

There were no significant spending variances during the first quarter in any major expense category of OIG budget component of the 2018 FDIC Operating Budget.

Significant Spending Variances by Division/Office[1]

No organizations had significant spending variances through the end of the first quarter.

Other Matters

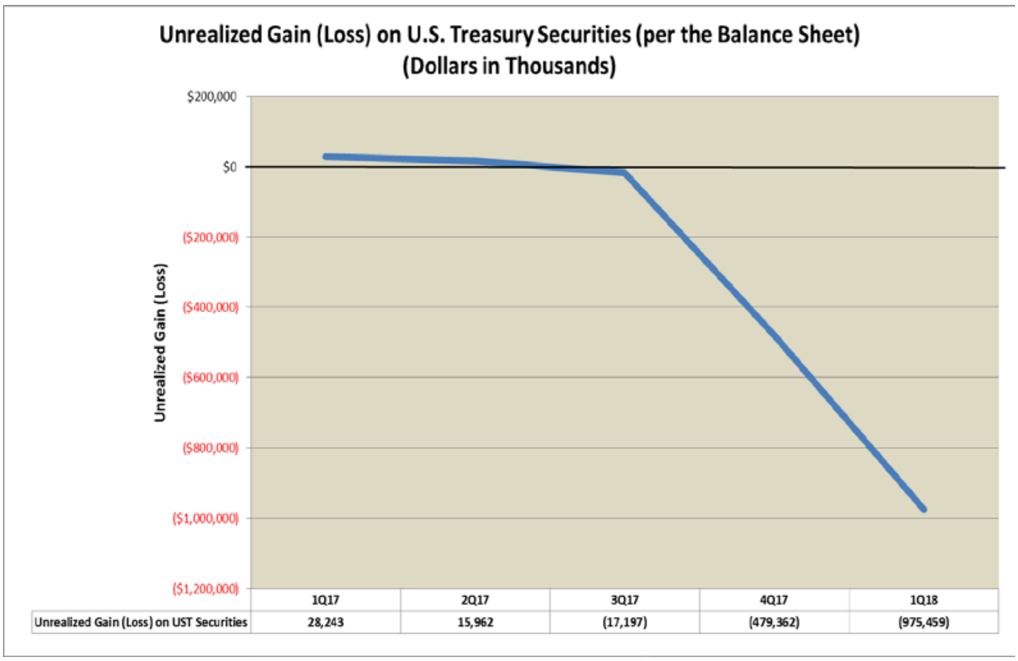
An updated analysis of 2018 funding requirements for employee pay and benefits was completed in March, in accordance with the 2018 Budget Resolution. The analysis determined that the projected costs related to fringe benefits had been overestimated during the preparation of the 2018 FDIC Operating Budget by approximately $3.2 million in the Salaries and Compensation expense category. This variance was primarily due to the inclusion of an expected small general fringe benefit cost increase that has not been fully experienced to date. The CFO elected not to exercise his delegated authority to adjust the 2018 FDIC Operating Budget to address this variance, since the net projected budget difference is not material to the total amount of the 2018 Salaries and Compensation budget or to the overall 2018 FDIC Operating Budget.

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

Fund Financial Results

($ in Millions)

Balance Sheet	Deposit Insurance Fund				
	Mar-18	Dec-17	Quarterly Change	Mar-17	Year-Over-Year Change
Cash and cash equivalents	$ 3,119	$ 1,829	$ 1,290	$ 3,374	$ (255)
Investment in U.S. Treasury securities	84,831	83,303	1,528	75,076	9,755
Assessments receivable, net	2,783	2,634	149	2,709	74
Interest receivable on investments and other assets, net	581	506	75	458	123
Receivables from resolutions, net	5,194	5,973	(779)	6,760	(1,566)
Property and equipment, net	325	334	(9)	340	(15)
Total Assets	$ 96,833	$ 94,579	$ 2,254	$ 88,717	$ 8,116
Accounts payable and other liabilities	200	237	(37)	208	(8)
Liabilities due to resolutions	1,154	1,203	(49)	2,011	(857)
Postretirement benefit liability	259	259	-	232	27
Contingent liability for anticipated failures	113	98	15	1,335	(1,222)
Contingent liability for litigation losses and other	35	35	0	3	32
Total Liabilities	$ 1,761	$ 1,832	$ (71)	$ 3,789	$ (2,028)
FYI: Unrealized gain (loss) on U.S. Treasury securities, net	(975)	(479)	(496)	28	(1,003)
FYI: Unrealized postretirement benefit (loss) gain	(46)	(46)	-	(26)	(20)
Fund Balance	$ 95,072	$ 92,747	$ 2,325	$ 84,928	$ 10,144



The larger unrealized losses on the DIF portfolio's U.S. Treasury securities lately has been the result of yields continuing to rise dramatically across all maturity sectors of the Treasury yield curve, resulting in further declines in the securities' market values relative to their book values.

Fund Financial Results - continued

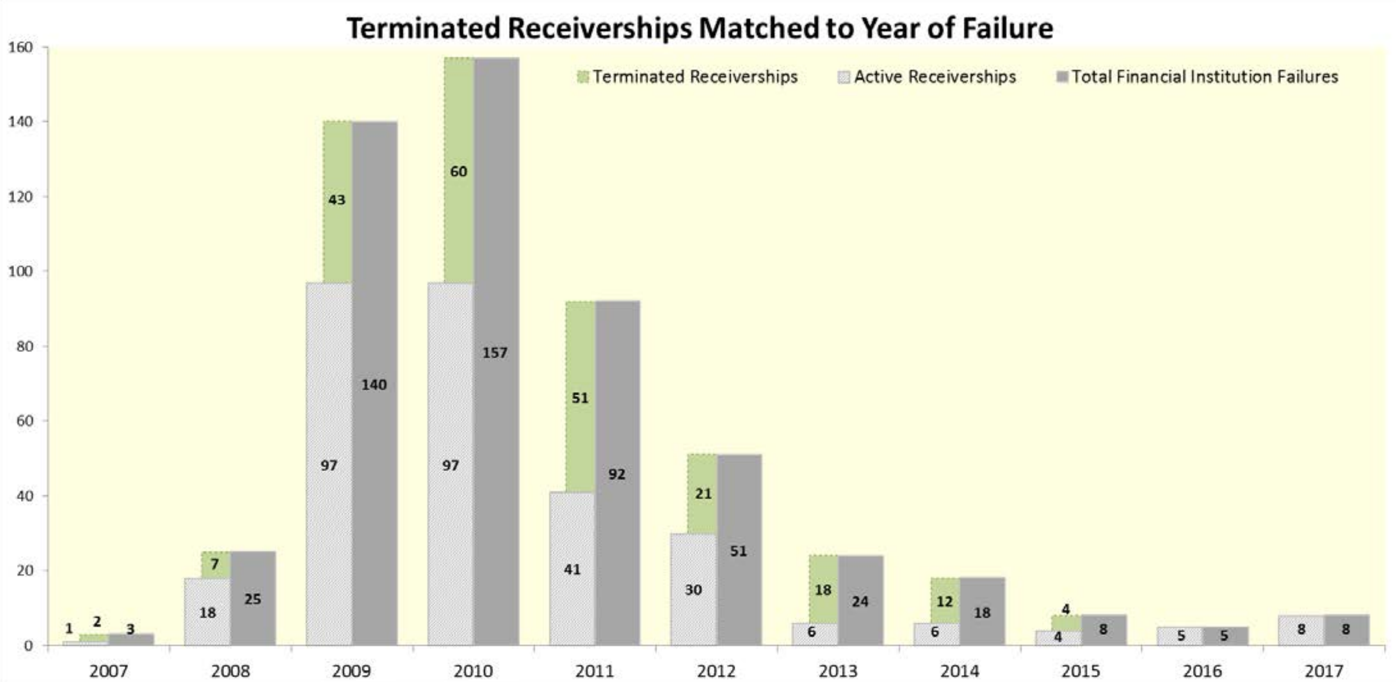
($ in Millions)

Income Statement (year-to-date)	Deposit Insurance Fund Mar-18	Dec-17		Mar-17	Year-Over-Year Change
Assessments	$ 2,850	$ 10,595		$ 2,737	$ 113
Interest on U.S. Treasury securities	338	1,057		227	111
Other revenue	1	12		2	(1)
Total Revenue	$ 3,189	$ 11,664		$ 2,966	$ 223
Operating expenses	433	1,740		442	(9)
Provision for insurance losses	(65)	(183)		765	(830)
Insurance and other expenses	0	2		0	0
Total Expenses and Losses	$ 368	$ 1,559		$ 1,207	$ (839)
Net Income	2,821	10,105		1,759	1,062
Unrealized gain (loss) on U.S. Treasury securities, net	(496)	(500)		7	(503)
Unrealized postretirement benefit gain (loss)	-	(20)		-	-
Comprehensive Income	$ 2,325	$ 9,585		$ 1,766	$ 559

Selected Financial Data	FSLIC Resolution Fund Mar-18	Dec-17	Quarterly Change	Mar-17	Year-Over-Year Change
Cash and cash equivalents	$ 889	$ 885	$ 4	$ 879	$ 10
Accumulated deficit	(124,601)	(124,604)	3	(124,609)	8
Total resolution equity	889	886	3	880	9
Total revenue	3	8		1	2
Operating expenses	0	1		0	0
Losses related to thrift resolutions	0	0		0	0
Net Income (Loss)	$ 3	$ 7		$ 1	2

Receivership Selected Statistics March 2018 vs. March 2017

$ in millions	DIF			FRF			ALL FUNDS		
	Mar-18	Mar-17	*Change*	Mar-18	Mar-17	*Change*	Mar-18	Mar-17	*Change*
Total Receiverships	317	375	(58)	-	-	-	317	375	(58)
Assets in Liquidation	$ 2,097	$ 3,006	$ (909)	$ 2	$ 2	-	$ 2,099	$ 3,008	$ (909)
YTD Collections	$ 492	$ 379	$ 113	-	-	$ -	$ 492	$ 379	$ 113
YTD Dividend/Other Pymts - Cash	$ 847	$ 1,203	$ (356)	-	-	-	$ 847	$ 1,203	$ (356)



The FDIC, as receiver, manages failed banks with the goal of expeditiously winding up their affairs. The oversight and prompt termination of receiverships help to preserve value for the uninsured depositors and other creditors by reducing overhead and other holding costs. Once the assets of a failed institution have been sold, the final distribution of any proceeds is made and the FDIC terminates the receivership. As of March 31, 2018, the FDIC has inactivated 218 receiverships (or 41 percent) of the 531 receiverships created from 2007 through 2017.

Deposit Insurance Fund Portfolio Summary

(Dollar Values in Millions)

	3/31/18	12/31/17	Change
Par Value	$88,749	$85,376	$3,373
Amortized Cost	$89,002	$85,707	$3,295
Total Market Value (including accrued interest)	$88,477	$85,590	$2,887
Primary Reserve [1]	$88,477	$85,590	$2,887
Primary Reserve % of Total Portfolio	100.0%	100.0%	0.0%
Yield-to-Maturity [2]	1.63%	1.52%	0.11%
Weighted Average Maturity (in years)	1.97	2.05	-0.08
Effective Duration (in years)			
Total Portfolio	1.90	1.97	-0.07
Available-for-Sale Securities	1.99	2.07	-0.08
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 (AFS) securities, 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)

	3/31/18	12/31/17	Change
FRF-FSLIC			
Book Value [4]	$845	$842	$3
Yield-to-Maturity	1.64%	1.20%	0.44%
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)

	3/31/18	12/31/17	Change
Book Value [5]	$4,363	$4,733	($370)
Effective Annual Yield	1.58%	1.24%	0.34%
Weighted Average Maturity (in days)	51	51	0

[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 2018** Purchase up to $11 billion (par value) of Treasury securities with maturity dates between June 30, 2018, and June 30, 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 target at least $3 billion (par value) of newly purchased securities maturing between July 1, 2021, and June 30, 2023.
	Strategy Changes for the 2nd Quarter 2018
	Purchase up to <u>$15 billion</u> (par value) of Treasury securities with maturity dates between <u>September 30, 2018</u>, and June 30, 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 target at least <u>$2 billion</u> (par value) of newly purchased securities maturing between July 1, 2021, and June 30, 2023.
NATIONAL LIQUIDATION FUND	**Strategy for the 1st Quarter 2018** 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 2018
	No strategy changes for the second quarter of 2018.

Executive Summary of 2018 Budget and Expenditures
by Budget Component and Major Expense Category
Through March 31, 2018
(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	$1,234,811	$317,407	$299,024	94%	($18,383)
Outside Services - Personnel	271,788	57,641	52,131	90%	(5,510)
Travel	92,677	22,855	20,990	92%	(1,865)
Buildings	104,832	24,147	21,798	90%	(2,349)
Equipment	93,364	16,148	16,496	102%	348
Outside Services - Other	16,197	3,397	3,121	92%	(276)
Other Expenses	13,366	3,188	3,375	106%	187
Total Ongoing Operations	**$1,827,035**	**$444,783**	**$416,935**	**94%**	**($27,848)**
Receivership Funding					
Salaries & Compensation	$21,690	$6,232	$4,521	73%	($1,711)
Outside Services - Personnel	183,300	39,674	37,452	94%	(2,222)
Travel	3,574	887	593	67%	(294)
Buildings	6,968	1,739	1,342	77%	(397)
Equipment	969	271	148	55%	(123)
Outside Services - Other	1,327	328	402	123%	74
Other Expenses	7,172	1,791	336	19%	(1,455)
Total Receivership Funding	**$225,000**	**$50,922**	**$44,794**	**88%**	**($6,128)**
Office of Inspector General					
Salaries & Compensation	$34,853	$8,713	$8,169	94%	($544)
Outside Services - Personnel	1,660	415	346	83%	(69)
Travel	1,583	396	219	55%	(177)
Buildings	0	0	0		0
Equipment	1,555	389	83	21%	(306)
Outside Services - Other	0	0	0		0
Other Expenses	447	112	23	21%	(89)
Total Office of Inspector General	**$40,098**	**$10,025**	**$8,840**	**88%**	**($1,185)**
Total FDIC Operating Budget	**$2,092,133**	**$505,730**	**$470,569**	**93%**	**($35,161)**

Executive Summary of 2018 Budget and Expenditures by Division/Office Through March 31, 2018 (Dollars in Thousands)					
Division/Office	Annual Budget	YTD Budget	YTD Expenditures	% of YTD Budget Used	YTD Variance
FDIC Operating Budget					
Risk Management Supervision	$593,176	$151,957	$141,893	93%	($10,064)
Administration	278,660	68,929	63,581	92%	(5,348)
Resolutions & Receiverships	238,195	61,292	54,157	88%	(7,135)
Information Technology	222,167	44,965	45,493	101%	528
Legal	201,429	51,554	48,627	94%	(2,927)
Depositor & Consumer Protection	186,468	48,149	42,925	89%	(5,224)
Insurance & Research	51,855	12,960	12,536	97%	(424)
CIO Council	51,086	10,879	10,019	92%	(860)
Information Security & Privacy Staff	44,203	10,525	10,055	96%	(470)
Finance	40,851	10,404	10,009	96%	(395)
Inspector General	40,098	10,025	8,840	88%	(1,185)
Executive Support [1]	22,875	5,512	5,067	92%	(445)
Corporate University - Corporate	21,773	5,952	6,673	112%	721
Complex Financial Institutions	21,063	4,876	4,468	92%	(408)
Corporate University - CEP	19,345	4,647	3,972	85%	(675)
Executive Offices [2]	11,073	3,104	2,254	73%	(850)
Corporate Unassigned	47,816	0	0		0
Total FDIC Operating Budget	**$2,092,133**	**$505,730**	**$470,569**	**93%**	**($35,161)**

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.