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

November 17, 2017

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: Third Quarter 2017 CFO Report to the Board

The attached report highlights the FDIC's financial activities and results for the quarter ended September 30, 2017.

Executive Summary

- During the third quarter of 2017, the Deposit Insurance Fund (DIF) balance increased by $2.9 billion, from $87.6 billion at June 30, 2017 to $90.5 billion at September 30, 2017. The quarterly increase was primarily due to $2.6 billion of assessment revenue, $274 million of interest on U.S. Treasury securities, and a $512 million decrease in provision for insurance losses, partially offset by $404 million of operating expenses.

- The reserve ratio, which is the ratio of the DIF balance to estimated insured deposits, was 1.28 percent for the third quarter 2017, compared to the second quarter 2017 reserve ratio of 1.24 percent.

- There were no financial institution failures during the third quarter of 2017.

- Through September 30, 2017, overall FDIC Operating Budget expenditures were below budget by 8 percent ($119 million). This variance was primarily the result of higher than expected vacancies in budgeted positions during the year. In addition, lower-than-anticipated expenses for facilities, outside legal counsel, and other outside services contributed to the variance.

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

Deposit Insurance Fund

- For the nine months ending September 30, 2017, the DIF's comprehensive income totaled $7.3 billion compared to comprehensive income of $8.1 billion for the same period last year. This $760 million decline was primarily the result of a $1.3 billion increase in provision for insurance losses (year-to-date 2017 positive $20 million versus year-to-date 2016 negative $1.2 billion) and a $393 million lower contribution to year-to-date comprehensive income from unrealized (loss)/gain on U.S. Treasury securities (year-to-date 2017 unrealized loss of $38 million versus year-to-date 2016 unrealized gain of $355 million), partially offset by a $640 million increase in assessment revenue and a $270 million increase in interest revenue.

- The provision for insurance losses was $20 million for year-to-date 2017, compared to negative $1.2 billion for year-to-date 2016. The provision for 2017 primarily resulted from a decrease of $702 million to the estimated losses for prior year failures offset by a $683 million adjustment for higher-than-anticipated losses at the time of failure for current year failures, as compared to the estimated liability at year-end 2016. Reductions for estimated losses for prior year failures occurred in both periods; however, the decreases in 2016 were approximately 40 percent more than those in 2017 ($702 million for year-to-date 2017 and $1.2 billion for year-to-date 2016).

Assessments

- During September, the DIF recognized assessment revenue of $2.6 billion. Of this amount, $1.4 billion represented the estimate for the third quarter 2017 insurance coverage and $1.2 billion represented estimated assessment surcharges on banks with $10 billion or more in assets. Additionally, the DIF recognized a $67 million adjustment for lower-than-estimated collections for the second quarter 2017 insurance coverage (regular assessments and surcharges), which decreased assessment revenue.

- On September 29, 2017, the FDIC collected $1.4 billion in DIF regular assessments and $1.2 billion in surcharge assessments for second quarter 2017 insurance coverage.

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

DIF Investment Portfolio

- On September 30, 2017, the total liquidity (also total market value) of the DIF investment portfolio stood at $81.2 billion, up $5.9 billion from its December 31, 2016, balance of $75.3 billion. During the first three quarters of the year, interest revenue, receivership dividends, and deposit insurance assessment collections exceeded resolution-related outlays and operating expenses.

- On September 30, 2017, the DIF investment portfolio's yield was 1.42 percent, up 30 basis points from its 1.12 percent yield on December 31, 2016. The new Treasury securities purchased during the first three quarters of the year generally had higher yields than the maturing securities' yields, some considerably higher.

- In accordance with the approved third quarter 2017 DIF portfolio investment strategy, staff purchased a total of 19 short- to intermediate-maturity conventional Treasury securities, all designated as available-for-sale. The 19 securities had a total par value of $10.2 billion, a weighted average yield of 1.56 percent, and a weighted average maturity of 2.73 years.

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

Approved Budget Modifications

The 2017 Budget Resolution delegated to the Chief Financial Officer (CFO) and selected other officials the authority to make certain modifications to the 2017 FDIC Operating Budget. The following budget reallocations were approved during the third quarter in accordance with the authority delegated by the Board of Directors.

- In July 2017, the Division of Administration (DOA) implemented an internal realignment of its existing Ongoing Operations budget to increase the Buildings expense category by $1,878,500 and decrease the Equipment and Outside Services-Personnel expense categories by $1,159,500 and $719,000, respectively.

- In August 2017, the CFO approved the following budget increases and realignments, primarily through the realignment of funds from the Corporate Unassigned contingency reserve:

    - An increase of $116,500 to the Outside Services-Personnel expense category of the Ongoing Operation budget of the Division of Information Technology (DIT). This increase provided continuing contract support for the CIO's internal communications program.

    - An increase of $533,319 to the Outside Services-Personnel expense category of the Ongoing Operations budget of DIT to complete a Phase I pilot of the Data Protection Program (planning funds for this initiative were included in the initial 2017 DIT Ongoing Operations budget). This program will protect FDIC data by developing standards for classification of data, assigning classifications to all FDIC information, and implementing tools to secure data according to its classification.

- Following all third quarter budget modifications, the balances in the Corporate Unassigned contingency reserves were $25,764,771 in the Ongoing Operations budget component and $30,524,390 in the Receivership Funding budget component.

Approved Staffing Modifications

The 2017 Budget Resolution delegated to the CFO the authority to modify approved 2017 staffing authorizations for divisions and offices, as long as those modifications did not increase the total approved 2017 FDIC Operating Budget. There were no approved staffing modifications in the third quarter.

Spending Variances

Significant spending variances by major expense category and division/office are discussed below. Significant spending variances for the nine months ending September 30, 2017, are defined as those that either (1) exceed the YTD budget by more than $1 million and represent more than two 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 $7 million and represents more than seven percent of the major expense category or total division/office budget.

Significant Spending Variances by Major Expense Category

<u>Ongoing Operations</u>

There was only one significant spending variance in a major expense category in the Ongoing Operations budget component through the third quarter:

- Expenditures for Equipment were $8.8 million, or 15% less than budgeted. This variance was largely attributable to lower-than-budgeted spending by the DIT on technology refreshment purchases and software maintenance.

Receivership Funding

The Receivership Funding component of the 2017 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 was only one significant spending variance in a major expense category in the Receivership Funding budget component through the third quarter:

- Outside Services-Personnel expenditures were $22.5 million, or 15 percent, less than budgeted. This variance was mostly attributable to lower-than-budgeted spending for outside counsel services by the Legal Division, which spent $20 million, or 35 percent, less than budgeted. The Legal Division attributes this underspending to the significant amount of litigation that was on hold while waiting for the court to rule on motions.

Office of Inspector General

There were no significant spending variances through the third quarter in any major expense category of the Office of Inspector General budget component of the 2017 FDIC Operating Budget.

Significant Spending Variances by Division/Office[1]

Two organizations had significant spending variances through the end of the third quarter:

- The Legal Division spent $29 million, or 17%, less than budgeted, due mostly to a lower-than-anticipated use of outside legal counsel in the Receivership Funding component and due to vacancies in budgeted staffing positions.

- DOA spent $15 million, or 8%, less than budgeted, largely due to lower-than-budgeted spending on building operating costs, maintenance and repairs, and construction projects that have been deferred, partially or wholly, to 2018. Additionally, lower spending for security services from Global Resource Solutions, Inc. and the Office of Personnel Management contributed to the variance.

- The Division of Resolutions and Receiverships spent $14 million, or 7%, less than budgeted, largely due to lower than budgeted salaries and compensation expenses in both the Ongoing Operations and Receivership Funding budget components, and less than anticipated spending in the Buildings expense category of the Receivership Funding budget component.

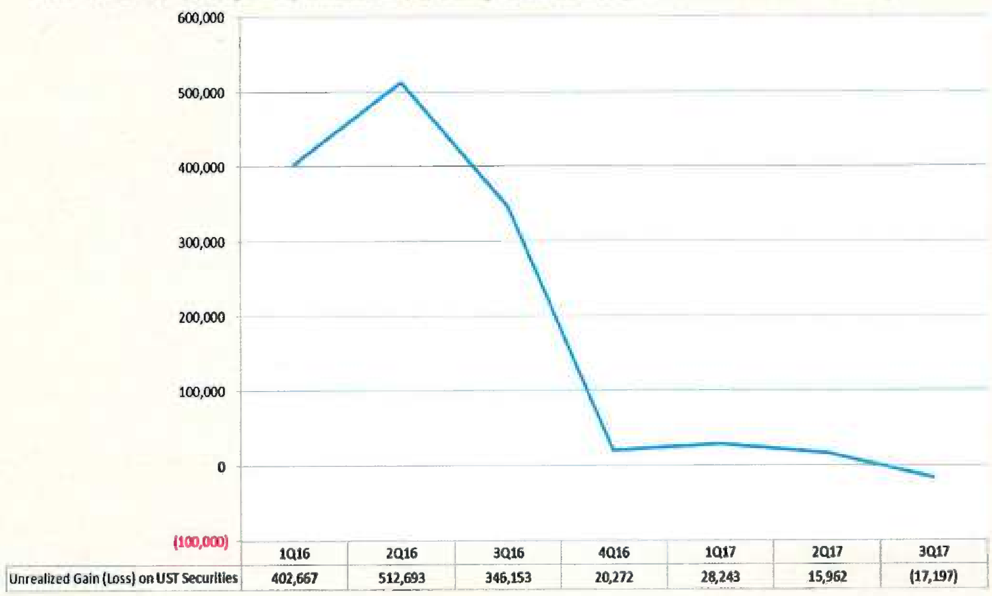
[1]Information on division/office variances reflects variances in the FDIC Operating Budget.

Fund Financial Results

($ in Millions)

Balance Sheet	Deposit Insurance Fund				
	Sep-17	Jun-17	Quarterly Change	Sep-16	Year-Over-Year Change
Cash and cash equivalents	$ 1,237	$ 3,362	$ (2,125)	$ 4,273	$ (3,036)
Investment in U.S. Treasury securities	79,439	75,043	4,396	68,124	11,315
Assessments receivable, net	2,635	2,677	(42)	2,686	(51)
Interest receivable on investments and other assets, net	517	399	118	565	(48)
Receivables from resolutions, net	9,317	8,944	373	9,044	273
Property and equipment, net	333	324	9	360	(27)
Total Assets	$ 93,478	$ 90,749	$ 2,729	$ 85,052	$ 8,426
Accounts payable and other liabilities	198	242	(44)	218	(20)
Liabilities due to resolutions	2,421	2,535	(114)	3,538	(1,117)
Postretirement benefit liability	232	232	-	233	(1)
Contingent liability for anticipated failures	86	117	(31)	359	(273)
Contingent liability for litigation losses and other	35	35	0	0	35
Total Liabilities	$ 2,972	$ 3,161	$ (189)	$ 4,348	$ (1,376)
FYI: Unrealized gain (loss) on U.S. Treasury securities, net	(17)	16	(33)	346	(363)
FYI: Unrealized postretirement benefit (loss) gain	(26)	(26)	-	(34)	8
Fund Balance	$ 90,506	$ 87,588	$ 2,918	$ 80,704	$ 9,802

Unrealized Gain (Loss) on U.S. Treasury Securities (per the Balance Sheet)



The decrease in unrealized gains on the DIF portfolio's U.S. Treasury securities since mid-2016 was the result of yields rising dramatically across all maturity sectors of the Treasury yield curve, resulting in declines in the securities' market values relative to their book values.

Fund Financial Results - continued

($ in Millions)

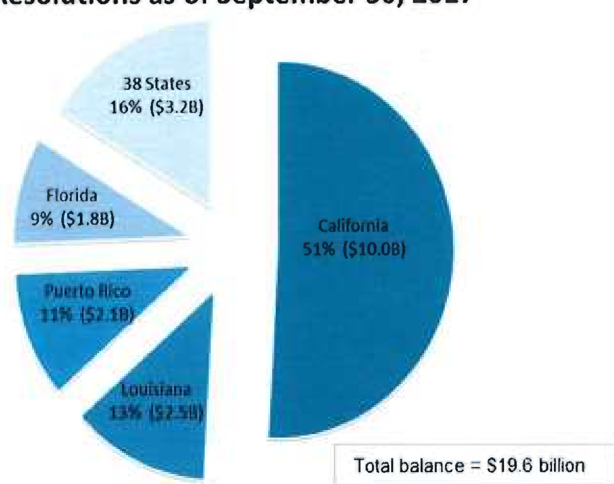
Income Statement (year-to-date)	Deposit Insurance Fund Sep-17	Jun-17	Quarterly Change	Sep-16	Year-Over-Year Change
Assessments	$ 7,939	$ 5,371	$ 2,568	$ 7,299	$ 640
Interest on U.S. Treasury securities	752	478	274	482	270
Other revenue	8	6	2	13	(5)
Total Revenue	$ 8,699	$ 5,855	$ 2,844	$ 7,794	$ 905
Operating expenses	1,296	892	404	1,278	18
Provision for insurance losses	20	532	(512)	(1,236)	1,256
Insurance and other expenses	1	0	1	3	(2)
Total Expenses and Losses	$ 1,317	$ 1,424	$ (107)	$ 45	$ 1,272
Net Income	7,382	4,431	$ 2,951	7,749	(367)
Unrealized gain (loss) on U.S. Treasury securities, net	(38)	(5)	(33)	355	(393)
Unrealized postretirement benefit gain (loss)	-	-	-	-	-
Comprehensive Income	$ 7,344	$ 4,426	$ 2,918	$ 8,104	$ (760)

Selected Financial Data	FSLIC Resolution Fund Sep-17	Jun-17	Quarterly Change	Sep-16	Year-Over-Year Change
Cash and cash equivalents	$ 883	$ 881	$ 2	$ 873	$ 10
Accumulated deficit	(124,606)	(124,607)	1	(124,616)	10
Total resolution equity	884	882	2	873	11
Total revenue	5	3	2	4	1
Operating expenses	0	0	0	3	(3)
Losses related to thrift resolutions	0	0	0	0	0
Net Income (Loss)	$ 5	$ 3	2	$ 2	3

Receivership Selected Statistics September 2017 vs. September 2016

$ in millions	DIF			FRF			ALL FUNDS		
	Sep-17	Sep-16	*Change*	Sep-17	Sep-16	*Change*	Sep-17	Sep-16	*Change*
Total Receiverships	367	404	(37)	-	-	-	367	404	(37)
Assets in Liquidation	$ 4,971	$ 3,756	$ 1,215	$ 2	$ 2	$ -	$ 4,973	$ 3,758	$ 1,215
YTD Collections	$ 1,260	$ 1,289	$ (29)	$ 1	$ 2	$ (1)	$ 1,261	$ 1,291	$ (30)
YTD Dividend/Other Pymts - Cash	$ 1,448	$ 3,296	$ (1,848)	$ -	$ -	$ -	$ 1,448	$ 3,296	$ (1,848)

Concentration of Credit Risk in Receivables from Resolutions as of September 30, 2017



The repayment of the receivables from resolutions is primarily influenced by recoveries on assets held by DIF receiverships and receivership payments on the covered assets under shared-loss agreements. The majority of the remaining assets in liquidation ($5.0 billion) and current shared-loss covered assets ($14.6 billion), which together total $19.6 billion, are concentrated in failed institutions located in California, Louisiana, Puerto Rico, and Florida.

Of the $19.6 billion total balance, $16.4 billion (84%) is concentrated in California, Louisiana, Puerto Rico, and Florida.

Deposit Insurance Fund Portfolio Summary (Dollar Values in Millions)			
	9/30/17	12/31/16	Change
Par Value	$80,233	$74,430	$5,803
Amortized Cost	$80,766	$74,947	$5,819
Total Market Value (including accrued interest)	$81,152	$75,335	$5,817
Primary Reserve [1]	$81,152	$75,335	$5,817
Primary Reserve % of Total Portfolio	100.0%	100.0%	0.0%
Yield-to-Maturity [2]	1.42%	1.12%	0.30%
Weighted Average Maturity (in years)	1.98	1.60	0.38
Effective Duration (in years)			
Total Portfolio	1.91	1.55	0.36
Available-for-Sale Securities	1.98	1.66	0.32
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 yield of 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)			
	9/30/17	12/31/16	Change
FRF-FSLIC			
Book Value [4]	$839	$831	$8
Yield-to-Maturity	0.97%	0.40%	0.57%
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)			
	9/30/17	12/31/16	Change
Book Value [5]	$5,890	$8,746	($2,856)
Effective Annual Yield	0.95%	0.58%	0.37%
Weighted Average Maturity (in days)	34	78	(44)

[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 3rd Quarter 2017** Purchase up to $13 billion (par value) of Treasury securities with maturity dates between December 31, 2017, and December 31, 2022, 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 $4 billion (par value) of newly purchased securities maturing between July 1, 2020, and December 31, 2022.
	Strategy Changes for the 4th Quarter 2017
	Purchase up to <u>$11 billion</u> (par value) of Treasury securities with maturity dates between <u>March 31, 2018</u>, and December 31, 2022, 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 $4 billion (par value) of newly purchased securities maturing <u>in 2021 or 2022</u>.
NATIONAL LIQUIDATION FUND	**Strategy for the 3rd Quarter 2017** 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 4th Quarter 2017
	No strategy changes for the fourth quarter of 2017.

Executive Summary of 2017 Budget and Expenditures by Budget Component and Major Expense Category Through September 30, 2017 (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	$1,247,608	$923,078	$874,351	95%	($48,727)
Outside Services - Personnel	$253,201	$178,734	$166,824	93%	($11,910)
Travel	$95,448	$70,897	$65,008	92%	($5,889)
Buildings	$103,054	$73,625	$68,221	93%	($5,404)
Equipment	$91,133	$58,256	$49,489	85%	($8,767)
Outside Services - Other	$16,545	$12,614	$11,227	89%	($1,387)
Other Expenses	$14,081	$10,308	$9,146	89%	($1,162)
Total Ongoing Operations	**$1,821,070**	**$1,327,512**	**$1,244,266**	**94%**	**($83,246)**
Receivership Funding					
Salaries & Compensation	$37,356	$27,898	$22,953	82%	($4,945)
Outside Services - Personnel	$230,152	$150,007	$127,500	85%	($22,507)
Travel	$3,284	$2,442	$3,232	132%	$790
Buildings	$17,700	$13,308	$6,937	52%	($6,371)
Equipment	$1,431	$618	$555	90%	($63)
Outside Services - Other	$1,273	$985	$1,075	109%	$90
Other Expenses	$8,804	$6,603	$5,292	80%	($1,311)
Total Receivership Funding	**$300,000**	**$201,861**	**$167,544**	**83%**	($34,317)
Office of Inspector General					
Salaries & Compensation	$32,770	$24,578	$23,351	95%	($1,227)
Outside Services - Personnel	$1,418	$1,063	$837	79%	($226)
Travel	$1,486	$1,114	$1,000	90%	($114)
Buildings	$0	$0	$0		$0
Equipment	$487	$365	$456	125%	$91
Outside Services - Other	$169	$127	$7	6%	($120)
Other Expenses	$423	$317	$305	96%	($12)
Total Office of Inspector General	**$36,753**	**$27,564**	**$25,956**	**94%**	**($1,608)**
Total FDIC Operating Budget	**$2,157,823**	**$1,556,937**	**$1,437,766**	**92%**	**($119,171)**

Executive Summary of 2017 Budget and Expenditures by Division/Office Through September 30, 2017 (Dollars in Thousands)					
Division/Office	Annual Budget	YTD Budget	YTD Expenditures	% of YTD Budget Used	YTD Variance
FDIC Operating Budget					
Risk Management Supervision	$591,543	$440,174	$416,142	95%	($24,032)
Administration	$273,360	$202,355	$187,020	92%	($15,334)
Resolutions & Receiverships	$271,786	$203,421	$188,973	93%	($14,448)
Legal	$233,804	$174,960	$145,488	83%	($29,473)
Information Technology	$225,561	$161,290	$151,382	94%	($9,908)
Depositor & Consumer Protection	$181,141	$135,767	$128,983	95%	($6,785)
Insurance & Research	$53,106	$39,541	$36,154	91%	($3,386)
CIO Council	$50,362	$35,773	$33,979	95%	(1,794)
Chief Information Security Officer [1]	$41,969	$30,006	$24,991	83%	($5,015)
Finance	$40,548	$30,353	$28,570	94%	($1,783)
Inspector General	$36,753	$27,565	$25,956	94%	($1,608)
Executive Support [2]	$26,207	$19,164	$16,846	88%	($2,318)
Corporate University - Corporate	$25,133	$18,805	$18,021	96%	($785)
Complex Financial Institutions	$20,156	$14,896	$13,063	88%	($1,833)
Corporate University - CEP	$19,082	$14,580	$14,697	101%	$117
Executive Offices [3]	$11,023	$8,287	$7,501	91%	($786)
Corporate Unassigned	$56,289	$0	$0		$0
Total FDIC Operating Budget	**$2,157,823**	**$1,556,937**	**$1,437,766**	**92%**	**($119,171)**

1) The Information Security & Privacy Staff was renamed the Office of the Chief Information Security Officer.

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

3) 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.