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

December 6, 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: Third Quarter 2018 CFO Report to the Board

The attached report highlights the FDIC's financial activities and results for the quarter ended September 30, 2018.

Executive Summary

- During the third quarter of 2018, the Deposit Insurance Fund (DIF) balance increased by $2.6 billion, from $97.6 billion at June 30, 2018, to $100.2 billion at September 30, 2018. The quarterly increase was primarily due to $2.7 billion of assessment revenue.

- The reserve ratio reached 1.36 percent as of September 30, 2018, exceeding the statutorily required minimum reserve ratio of 1.35 percent ahead of the September 30, 2020, deadline required under the Dodd-Frank Wall Street Reform and Consumer Protection Act. As a result, FDIC regulations provide for two changes to deposit insurance assessments upon reaching the minimum: (1) surcharges on insured depository institutions with total consolidated assets of $10 billion or more (large banks) will cease; and (2) small banks will receive assessment credits for the portion of their assessments that contributed to the growth in the reserve ratio from 1.15 percent to 1.35 percent, to be applied in any quarter that the reserve ratio is at or above 1.38 percent.

- There were no financial institution failures during the third quarter of 2018; the last failure occurred on December 15, 2017.

- Through September 30, 2018, overall FDIC Operating Budget expenditures were approximately 8 percent ($124.5 million) below budget. This variance was primarily the result of vacancies in budgeted positions, delays in purchasing equipment for the new backup data center, lower-than-budgeted spending for contractual services and outside legal counsel, and delays in building improvement projects.

I. **Financial Results** (See pages 6 – 7 for detailed data and charts.)

Deposit Insurance Fund

- During the nine months ending September 30, 2018, the DIF's comprehensive income totaled $7.5 billion compared to comprehensive income of $7.3 billion for the same period last year. The slight increase was largely the result of a $400 million increase in interest on U.S. Treasury securities, a $347 million decrease in provision for insurance losses, and a $237 million increase in assessment revenue. The increases were almost fully offset by an $854 million increase in unrealized losses on U.S. Treasury securities.

- The provision for insurance losses was a negative $327 million for the first nine months of 2018, compared to positive $20 million for the same period last year. The negative provision for 2018 primarily resulted from a $333 million decrease to the estimated losses for prior year failures. This adjustment was attributable to two primary components: a $181 million reduction to receivership shared-loss liability cost estimates resulting from lower-than-anticipated losses on covered assets, reductions in shared-loss cost estimates from the early termination of shared-loss agreements (SLAs) during the year, and unanticipated recoveries from SLAs where the commercial loss coverage has expired but the recovery period remains active; and $115 million of unanticipated recoveries from tax refunds, litigation settlements, and professional liability claims received by receiverships.

Assessments

- During September, the DIF recognized assessment revenue of $2.7 billion. Of this amount, $1.4 billion represented the estimate for the third quarter 2018 insurance coverage and $1.3 billion represented estimated surcharges on banks with $10 billion or more in assets. Additionally, the DIF recognized a $19 million adjustment, which increased assessment revenue.

- On September 28, 2018, the FDIC collected $1.4 billion in DIF regular assessments and $1.3 billion in surcharge assessments for second quarter 2018 insurance coverage.

II. **Investment Results** (See pages 8 – 9 for detailed data and charts.)

DIF Investment Portfolio

- On September 30, 2018, the total liquidity (also total market value) of the DIF investment portfolio stood at $95.5 billion, up $9.9 billion from its December 31, 2017, balance of $85.6 billion. During the year-to-date period, interest revenue, receivership dividends, and deposit insurance assessment collections far exceeded resolution-related outlays and operating expenses.

- On September 30, 2018, the DIF investment portfolio's yield was 1.92 percent, up 40 basis points from its 1.52 percent yield on December 31, 2017. The new Treasury securities purchased during the year-to-date period had higher yields than the maturing securities' yields.

- In accordance with the third quarter 2018 DIF portfolio investment strategy, staff purchased 21 short- to intermediate-maturity conventional Treasury securities, all designated as available-for-sale. The 21 securities had a total par value of $10.2 billion, a weighted average yield of 2.62 percent, and a weighted average maturity of 1.91 years.

III. **<u>Budget Results</u>** (See pages 10 – 11 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 third quarter in accordance with the authority delegated by the Board of Directors.

- In August, the Chief Information Officer (CIO) approved the reallocation of approximately $121,000 from the Outside Services – Personnel expense category to the Equipment expense category of the CIO Council budget to support the hosting and subscription costs for the Legal Division's Advanced Legal Information System.

- In September, the CFO approved budget changes in the Salary and Compensation budgets for most divisions and offices, based upon a Division of Finance review of corporate-wide spending in that expense category through August 2018. In the Ongoing Operations budget component, these reallocations resulted in reductions totaling approximately $18.1 million in the Salaries and Compensation budgets of individual divisions and offices to reflect unused spending through August. The funding was reallocated to the Corporate Unassigned contingency reserve. There were no changes within the Salary and Compensation expense category for the Receivership Funding budget component.

Following these budget modifications, the balances in the Corporate Unassigned contingency reserves as of September 30, 2018, were $20,634,877 in the Ongoing Operations budget component and $23,908,578 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 September, the Chairman announced a restructuring of the Executive Offices. This restructuring included the following changes:

    - Re-establishment of the position of Deputy to the Chairman for External Affairs.
    - Re-establishment of the position of Deputy to the Chairman for Policy.
    - Consolidation of the responsibilities of the Deputy to the Chairman and Chief Operating Officer (COO) and the Director, Division of Administration (DOA), into a single position.
    - Realignment of the Internal Ombudsman function and associated staff from the Office of the COO to DOA.
    - Realignment of one secretarial position from the Office of the COO to the Office of the Chairman.

  The restructuring resulted in a reduction of three authorized permanent positions (from 35 to 32) in the Executive Offices and an increase of five authorized permanent positions (from 372 to 377) in DOA.

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, 2018, 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 budget 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

Ongoing Operations

There were significant spending variances in three major expense categories of the Ongoing Operations budget component at the end of the third quarter:

Outside Services – Personnel expenditures were $18.7 million, or 10 percent, below budget. This was the result of under-spending by several organizations:

- The Division of Information Technology (DIT) spent $4.3 million less than budgeted due to delays in spending for contractor services related to migration to the new backup data center and reduced contractor expenses for infrastructure services.

- DOA spent $3.9 million less than budgeted due mostly to a lower-than-expected level of contractor support for human resources functions, underspending for guard services due to delays in on-boarding of new contractors, fewer-than-anticipated background investigations, and reduced expenses for the new Student Residence Center contract.

- The Office of Chief Information Security Officer (OCISO) spent $3.2 million less than budgeted due to deferred spending on multiple contracts, including those supporting the backup data center project.

- The CIO Council spent $2.2 million less than budgeted due to delays in starting development and enhancement projects and lower-than-projected expenses for systems maintenance and operations.

Equipment expenditures were $15.4 million, or 17%, under budget, mostly due to delays in equipment purchases for the backup data center and technology refreshment in DIT and OCISO.

Buildings expenditures were $12.3 million, or 16%, under budget due to procurement delays for four Headquarters building projects. Building improvement projects for the San Francisco Regional Office were also deferred, and reimbursements from the construction contractor for expenses related to a San Francisco Regional Office project were credited to the Buildings/Miscellaneous Operating account, which decreased total net expenses incurred for the year.

Receivership Funding

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 was a significant spending variance in one major expense category of the Receivership Funding budget component at the end of the third quarter. Spending for Outside Services - Personnel was $21 million, or 17%, below budget. This variance was mainly attributable to underspending for pre-closing and closing activities by the Division of Resolutions and Receiverships (DRR) because there have been no bank failures in 2018. Lower-than-anticipated expenses in the Legal Division for outside legal counsel services for receivership and resolution activities also contributed to this variance.

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.

Significant Spending Variances by Division/Office[1]

Five organizations had significant spending variances through the end of the third quarter.

- DRR spent $25 million, or 14%, less than budgeted, due mostly to lower than expected spending in the Outside Services – Personnel expense category of the Receivership Funding budget component. As noted above, this under-spending was attributable to the lack of institution failures this year.

- DOA spent $23 million, or 11%, less than budgeted, due largely to contract procurement delays in major building improvement projects at Headquarters buildings, deferred spending for building improvement projects at the San Francisco Regional Office, and fewer-than-anticipated interior improvements and construction projects at various other offices. DOA also contracted for fewer-than-expected background investigations and spent less for guard services due to delays in on-boarding of new contractors.

- DIT spent $16 million, or 9 percent, less than budgeted, mostly due to delays in the acquisition of equipment and contractual services for the backup data center, the replacement of obsolete equipment from the technology refreshment allowance, and spending for equipment maintenance and subscriptions. It also had lower-than-expected expenses for salaries due to vacancies in budgeted positions and for contracted infrastructure support services.

- Legal spent $14 million, or 10 percent, less than budgeted, due mainly to unfilled vacancies in budgeted positions and underspending for outside counsel services.

- OCISO spent $8 million, or 22 percent, less than budgeted, due mainly to delays in planned spending for equipment and services related to the backup data center project, lower-than-expected spending for other contractual services, and delays in the purchase of equipment from the technology refreshment allowance.

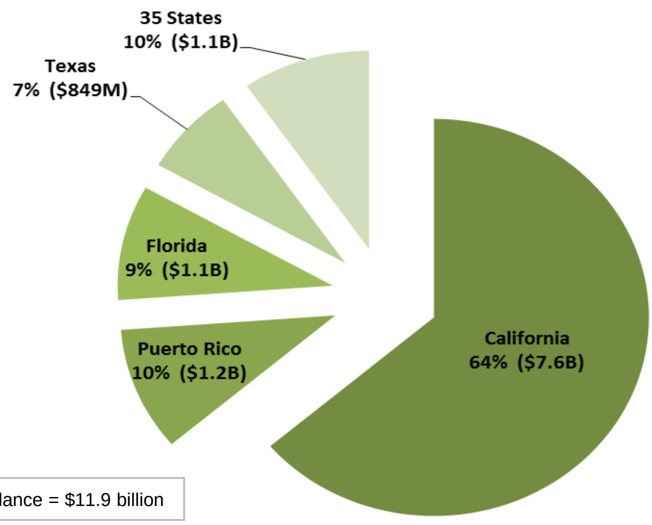
[1]Information on division/office variances reflects variances in the FDIC Operating Budget.

Fund Financial Results

($ in Millions)

Balance Sheet	Deposit Insurance Fund				
	Sep-18	Jun-18	Quarterly Change	Sep-17	Year-Over-Year Change
Cash and cash equivalents	$ 2,790	$ 3,535	$ (745)	$ 1,237	$ 1,553
Investment in U.S. Treasury securities	92,211	88,300	3,911	79,439	12,772
Assessments receivable, net	2,702	2,679	23	2,635	67
Interest receivable on investments and other assets, net	539	558	(19)	517	22
Receivables from resolutions, net	2,897	3,711	(814)	9,317	(6,420)
Property and equipment, net	322	321	1	333	(11)
Total Assets	$ 101,461	$ 99,104	$ 2,357	$ 93,478	$ 7,983
Accounts payable and other liabilities	204	232	(28)	198	6
Liabilities due to resolutions	654	905	(251)	2,421	(1,767)
Postretirement benefit liability	259	259	-	232	27
Contingent liability for anticipated failures	106	85	21	86	20
Contingent liability for guarantee payments and litigation losses	34	35	(1)	35	(1)
Total Liabilities	$ 1,257	$ 1,516	$ (259)	$ 2,972	$ (1,715)
FYI: Unrealized gain (loss) on U.S. Treasury securities, net	(1,371)	(1,137)	(234)	(17)	(1,354)
FYI: Unrealized postretirement benefit (loss) gain	(46)	(46)	-	(26)	(20)
Fund Balance	$ 100,204	$ 97,588	$ 2,616	$ 90,506	$ 9,698

Concentration of Credit Risk in Receivables from Resolutions as of September 30, 2018



Total balance = $11.9 billion

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 ($1.2 billion) and current shared-loss covered assets ($10.7 billion), which together total $11.9 billion, are concentrated in failed institutions located in California, Puerto Rico, Florida, and Texas.

Fund Financial Results - continued

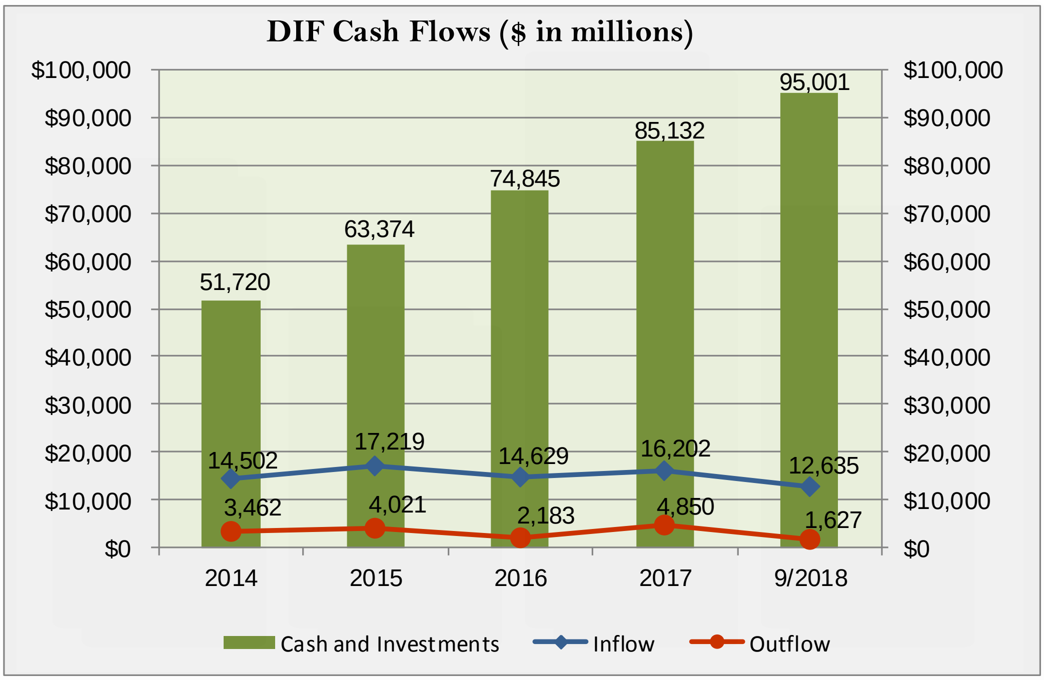
($ in Millions)

Income Statement (year-to-date)	Deposit Insurance Fund				
	Sep-18	Jun-18	Quarterly Change	Sep-17	Year-Over-Year Change
Assessments	$ 8,176	$ 5,448	$ 2,728	$ 7,939	$ 237
Interest on U.S. Treasury securities	1,152	719	433	752	400
Other revenue	8	5	3	8	0
Total Revenue	$ 9,336	$ 6,172	$ 3,164	$ 8,699	$ 637
Operating expenses	1,312	878	434	1,296	16
Provision for insurance losses	(327)	(206)	(121)	20	(347)
Insurance and other expenses	2	1	1	1	1
Total Expenses and Losses	$ 987	$ 673	$ 314	$ 1,317	$ (330)
Net Income	8,349	5,499	2,850	7,382	967
Unrealized gain (loss) on U.S. Treasury securities, net	(892)	(658)	(234)	(38)	(854)
Unrealized postretirement benefit gain (loss)	-	-	-	-	-
Comprehensive Income	$ 7,457	$ 4,841	$ 2,616	$ 7,344	$ 113

Selected Financial Data	FSLIC Resolution Fund				
	Sep-18	Jun-18	Quarterly Change	Sep-17	Year-Over-Year Change
Cash and cash equivalents	$ 896	$ 892	$ 4	$ 883	$ 13
Accumulated deficit	(124,593)	(124,597)	4	(124,606)	13
Total resolution equity	897	893	4	884	13
Total revenue	11	7	4	5	6
Operating expenses	0	0	0	0	0
Losses related to thrift resolutions	0	0	0	0	0
Net Income (Loss)	$ 11	$ 7	4	$ 5	6

Receivership Selected Statistics September 2018 vs. September 2017

$ in millions	DIF			FRF			ALL FUNDS		
	Sep-18	Sep-17	*Change*	Sep-18	Sep-17	*Change*	Sep-18	Sep-17	*Change*
Total Receiverships	282	367	(85)	-	-	-	282	367	(85)
Assets in Liquidation	$1,245	$ 4,971	$ (3,726)	$ 2	$ 2	-	$ 1,247	$ 4,973	$ (3,726)
YTD Collections	$1,333	$ 1,260	$ 73	-	1	$ (1)	$ 1,333	$ 1,261	$ 72
YTD Dividend/Other Pymts - Cash	$3,185	$ 1,448	$ 1,737	-	-	-	$ 3,185	$ 1,448	$ 1,737



Cash and Investments increased by $43.3 billion from $51.7 billion at year-end 2014 to $95.0 billion at September 30, 2018. The increase was primarily due to assessment collections, interest on U.S. Treasury securities, and recoveries from resolutions, that far exceeded resolution-related outlays and operating expenses.

Deposit Insurance Fund Portfolio Summary

(Dollar Values in Millions)

	9/30/18	12/31/17	Change
Par Value	$96,526	$85,376	$11,150
Amortized Cost	$96,458	$85,707	$10,751
Total Market Value (including accrued interest)	$95,491	$85,590	$9,901
Primary Reserve [1]	$95,491	$85,590	$9,901
Primary Reserve % of Total Portfolio	100.0%	100.0%	0.0%
Yield-to-Maturity [2]	1.92%	1.52%	0.40%
Weighted Average Maturity (in years)	1.83	2.05	-0.22
Effective Duration (in years)			
Total Portfolio	1.76	1.97	-0.21
Available-for-Sale Securities	1.85	2.07	-0.22
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)

	9/30/18	12/31/17	Change
FRF-FSLIC			
Book Value [4]	$852	$842	$10
Yield-to-Maturity	2.13%	1.20%	0.93%
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)

	9/30/18	12/31/17	Change
Book Value [5]	$3,025	$4,733	($1,708)
Effective Annual Yield	2.08%	1.24%	0.84%
Weighted Average Maturity (in days)	50	51	(1)

[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 2018** Purchase up to $13 billion (par value) of Treasury securities with maturity dates between December 31, 2018, 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 target at least $2 billion (par value) of newly purchased securities maturing between January 1, 2022, and December 31, 2023. **Strategy Changes for the 4th Quarter 2018** Purchase up to $14 billion (par value) of Treasury securities with maturity dates between March 31, 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 target at least $3.5 billion (par value) of newly purchased securities maturing between January 1, 2022, and December 31, 2023.
NATIONAL LIQUIDATION FUND	**Strategy for the 3rd 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 4th Quarter 2018** No strategy changes for the fourth quarter of 2018.

Executive Summary of 2018 Budget and Expenditures by Budget Component and Major Expense Category Through September 30, 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	$1,227,402	$915,979	$878,849	96%	($37,130)
Outside Services - Personnel	256,567	188,325	169,591	90%	(18,734)
Travel	92,754	69,568	66,409	95%	(3,159)
Buildings	106,307	78,104	65,802	84%	(12,302)
Equipment	114,441	89,506	74,110	83%	(15,396)
Outside Services - Other	16,196	12,198	11,611	95%	(587)
Other Expenses	13,368	9,696	8,778	91%	(918)
Total Ongoing Operations	**$1,827,035**	**$1,363,376**	**$1,275,150**	**94%**	**($88,226)**
Receivership Funding					
Salaries & Compensation	$19,390	$15,706	$10,498	67%	($5,208)
Outside Services - Personnel	185,600	120,277	99,305	83%	(20,972)
Travel	3,574	2,676	1,432	54%	(1,244)
Buildings	6,968	5,231	3,982	76%	(1,249)
Equipment	969	568	472	83%	(96)
Outside Services - Other	1,327	998	911	91%	(87)
Other Expenses	7,172	5,377	2,050	38%	(3,327)
Total Receivership Funding	**$225,000**	**$150,833**	**$118,650**	**79%**	**($32,183)**
Office of Inspector General					
Salaries & Compensation	$34,853	$26,140	$23,852	91%	($2,288)
Outside Services - Personnel	1,660	1,245	1,156	93%	(89)
Travel	1,583	1,187	683	58%	(504)
Buildings	0	0	0		0
Equipment	1,555	1,167	173	15%	(994)
Outside Services - Other	0	0	0		0
Other Expenses	447	335	168	50%	(167)
Total Office of Inspector General	**$40,098**	**$30,074**	**$26,032**	**87%**	**($4,042)**
Total FDIC Operating Budget	**$2,092,133**	**$1,544,283**	**$1,419,832**	**92%**	**($124,451)**

Executive Summary of 2018 Budget and Expenditures by Division/Office Through September 30, 2018 (Dollars in Thousands)					
Division/Office	Annual Budget	YTD Budget	YTD Expenditures	% of YTD Budget Used	YTD Variance
FDIC Operating Budget					
Risk Management Supervision	$579,831	$437,344	$419,766	96%	($17,578)
Resolutions & Receiverships	236,786	178,570	153,997	86%	(24,573)
Administration	274,830	203,859	180,783	89%	(23,076)
Legal	197,518	149,938	135,617	90%	(14,321)
Information Technology	244,696	186,395	170,262	91%	(16,133)
Depositor & Consumer Protection	181,186	137,742	130,822	95%	(6,920)
Insurance & Research	51,532	38,610	37,482	97%	(1,128)
CIO Council	52,118	37,500	35,525	95%	(1,975)
Finance	40,935	30,509	29,545	97%	(964)
Inspector General	40,098	30,074	26,032	87%	(4,042)
Information Security & Privacy Staff	50,383	39,003	30,617	78%	(8,386)
Executive Support [1]	21,902	16,458	15,158	92%	(1,300)
Complex Financial Institutions	19,715	13,862	13,301	96%	(561)
Corporate University - Corporate	26,153	21,477	19,388	90%	(2,089)
Corporate University - CEP	18,834	14,519	14,229	98%	(290)
Executive Offices [2]	11,073	8,423	7,308	87%	(1,115)
Corporate Unassigned	44,543	0	0		0
Total FDIC Operating Budget	**$2,092,133**	**$1,544,283**	**$1,419,832**	**92%**	**($124,451)**

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.