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

August 30, 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: Second Quarter 2018 CFO Report to the Board

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

Executive Summary

- During the second quarter of 2018, the Deposit Insurance Fund (DIF) balance increased by $2.5 billion, from $95.1 billion at March 31, 2018 to $97.6 billion at June 30, 2018. The quarterly increase was primarily due to $2.6 billion of assessment revenue.

- The reserve ratio, which is the ratio of the DIF balance to estimated insured deposits, was 1.33 percent for second quarter 2018, compared to the first quarter 2018 reserve ratio of 1.30 percent.

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

- Through June 30, 2018, overall FDIC Operating Budget expenditures were below budget by 7 percent ($73 million). This variance was primarily the result of vacancies in budgeted positions, delays in purchasing equipment for the backup data center, and lower-than-budgeted spending for contractual services and outside legal counsel.

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

Deposit Insurance Fund

- For the six months ending June 30, 2018, the DIF's comprehensive income totaled $4.8 billion compared to comprehensive income of $4.4 billion for the same period last year. This $415 million increase was primarily the result of a $738 million decrease in provision for insurance losses and a $241 million increase in interest on U.S. Treasury securities, partially offset by a $653 million reduction to comprehensive income from unrealized losses on U.S. Treasury securities (year-to-date 2018 unrealized loss of $658 million versus year-to-date 2017 unrealized loss of $5 million).

- The provision for insurance losses was a negative $206 million for the first half of 2018, compared to a positive $532 million for the same period last year. The negative provision for 2018 primarily resulted from reductions to the estimated losses for prior year failures, whereas the positive provision for 2017 was largely attributable to higher-than-anticipated estimated losses for current year failures, as compared to the related contingent liability at year-end 2016.

- During the first half of 2018, DIF incurred a $658 million unrealized loss on its portfolio of U.S. Treasury securities as a result of yields rising considerably across all investable maturity sectors of the Treasury yield curve. This rise resulted in declines in the securities' market values relative to their book values.

Assessments

- During June, the DIF recognized assessment revenue of $2.6 billion. Of this amount, $1.4 billion represented the estimate for the second quarter 2018 insurance coverage and $1.3 billion represented estimated surcharges on banks with $10 billion or more in assets. Additionally, the DIF recognized an $81 million adjustment for lower-than-estimated collections for the first quarter 2018 insurance coverage (regular assessments: $75 million and surcharges: $6 million), which decreased assessment revenue. This adjustment was primarily due to lower-than-estimated assessment rates.

- On June 29, 2018, the FDIC collected $1.4 billion in DIF regular assessments and $1.3 billion in surcharge assessments for first quarter 2018 insurance coverage.

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

DIF Investment Portfolio

- On June 30, 2018, the total liquidity (also total market value) of the DIF investment portfolio stood at $92.3 billion, up $6.7 billion from its December 31, 2017, balance of $85.6 billion. During the first half of the year, interest revenue, receivership dividends, and deposit insurance assessment collections far exceeded resolution-related outlays and operating expenses.

- On June 30, 2018, the DIF investment portfolio's yield was 1.78 percent, up 26 basis points from its 1.52 percent yield on December 31, 2017. The new Treasury securities purchased during the first half of the year had higher yields than the maturing securities' yields.

- In accordance with the approved second quarter 2018 DIF portfolio investment strategy, staff purchased a total of 29 short- to intermediate-maturity conventional Treasury securities, all designated as available-for-sale. The 29 securities had a total par value of $11.9 billion, a weighted average yield of 2.49 percent, and a weighted average maturity of 2.23 years.

III. **Budget Results** (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 second quarter in accordance with the authority delegated by the Board of Directors.

- In April 2018, after the Division of Finance conducted a review of spending in the salary and compensation accounts during the first quarter, the CFO approved budget reallocations in all divisions and offices, except the Executive Offices. In the Ongoing Operations budget components, reductions totaling approximately $12.3 million were made in the Salaries and Compensation accounts of most organizations to reflect unused spending during the first quarter. The Salaries and Compensation accounts of Corporate University - Corporate were increased by $4.9 million to provide adequate budget resources for employees detailed during the year, and the remaining $7.4 million was reallocated to the Corporate Unassigned contingency reserve. In the Receivership Funding budget component, small reductions totaling $57,707 were made in the Salaries and Compensation accounts of three divisions and the funds reallocated to the Corporate Unassigned contingency reserve.

- In April 2018, the Board of Directors approved a reallocation of $28 million from the Corporate Unassigned contingency reserve to Division of Information Technology (DIT), Office of Chief Information Security Officer (OCISO), and the CIO Council in the Ongoing Operations budget component. The funds are to support the Backup Data Center project and are mostly in the Equipment, $17.2 million, and Outside Services – Personnel, $10.1 million, expense categories. The remaining funds were reallocated to DIT in the Travel and Buildings expense categories.

- In May 2018, the CFO approved a $3.1 million budget increase to the Ongoing Operations budget component of OCISO. Additional funding of $1.7 million was provided in the Equipment expense category to augment the annual allowance for Hardware Technology Refreshment, and $1.4 million was added to the Outside Services – Personnel expense category to support a variety of security initiatives to address FISMA findings, establish metrics and reporting systems, and enhance incident response capabilities. Funding was provided by reallocating almost $200,000 from the Outside Services – Personnel expense category of the DIT and $2.9 million from the Corporate Unassigned contingency reserve to OCISO.

- In June 2018, the CFO approved mid-year budget adjustments that reallocated budget authority among several divisions and the Corporate Unassigned contingency reserve, as well as among expense categories within the divisions. In the Ongoing Operations budget component, budgets were reduced for two organizations and increased for two others: the Division of Administration or DOA (decreased by $2.3 million), the Office of Complex Financial Institutions or OCFI (decreased by $1.0 million), DIT (increased by $1.2 million), and OCISO (increased by $200,000). The reduction in the DOA budget primarily reflected lower-than-expected costs for electrical equipment replacement and construction delays for the F Street HVAC Retrofit Project. The reduction in the OCFI budget was due to the postponement of advisory services for a securities-for-claims exchange project. DIT received additional Equipment funding to meet its Technology Refreshment requirements, and OCISO received additional Outside Services – Personnel funds to initiate a privacy continuous monitoring program. The Corporate Unassigned contingency reserve was increased by $1.9 million as a result of these adjustments. In the Receivership Funding budget component, a reallocation of $2.3 million was made from the Salary and Compensation expense category to the Outside Services – Personnel expense category within the Division of Resolutions and Receiverships. This reallocation reflected decreased estimates of overtime and larger-than-projected costs for contracts that support bank closings. This adjustment resulted in no change to the Receivership Funding Corporate Unassigned contingency reserve.

Following these budget modifications, the balances in the Corporate Unassigned contingency reserves as of June 30, 2018, were $2,486,270 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 April, following consultation with the Chairman, the CFO approved an increase of five permanent authorized positions in the Office of the Chief Information Officer (CIO) to support the establishment of an enterprise IT strategy function within that office.

Spending Variances

Significant spending variances by major expense category and division/office are discussed below. Significant spending variances for the six months ending June 30, 2018, are defined as those that either (1) exceed the YTD budget by more than $2 million and represent more than three 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 $10 million and represents more than ten percent of the major expense category or total division/office budget.

Significant Spending Variances by Major Expense Category

<u>Ongoing Operations</u>

There were two significant spending variances through the second quarter in major expense categories of the Ongoing Operations budget component of the 2018 FDIC Operating Budget:

Outside Services – Personnel expenditures were $14.4 million, or 12 percent, below budget. This was the result of under-spending by several organizations:

- DIT spent $3.8 million less than budgeted due to delays in beginning several initiatives, a delay in paying award fees for the infrastructure services contract, and under-accrual of expenses on certain contracts.

- The CIO Council spent $2.8 million less than budgeted due to delays in starting application remediation activities for the Backup Data Center project and lower-than-projected expenses for systems maintenance and operations.

- DOA spent $2.6 million less than budgeted for background investigations.

- The Division of Depositor and Consumer Protection deferred spending on several contracts until the second half of the year.

Equipment expenditures were $18.5 million under budget, mostly due to delays in equipment purchases for the backup data center and technology refreshment.

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

Office of Inspector General

There were no significant spending variances through the second quarter in any major expense category of the Office of Inspector General budget component of the 2018 FDIC Operating Budget.

Significant Spending Variances by Division/Office[1]

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

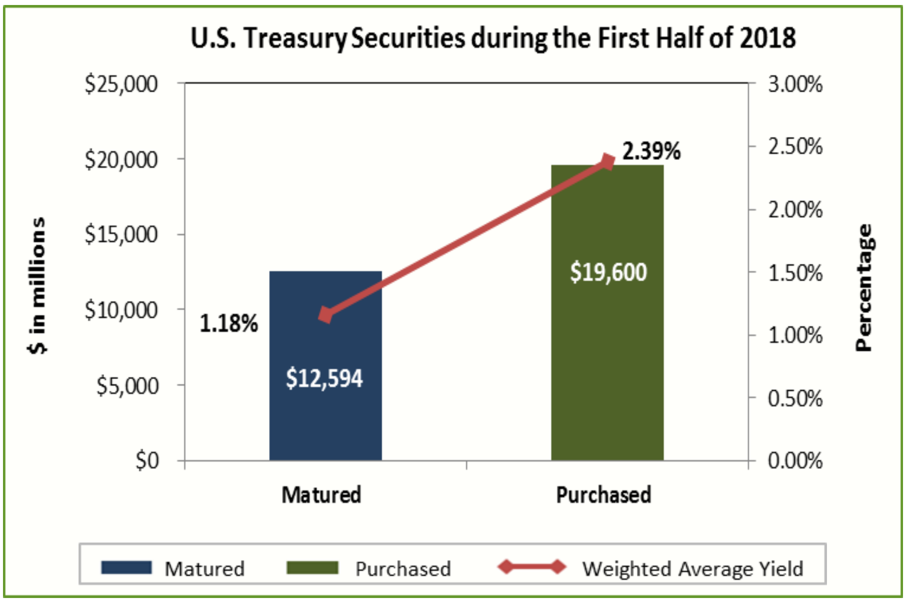
DIT had a significant spending variance of $21 million, or 17 percent, through the end of the second quarter, mostly due to delays in the acquisition of equipment and contractual services for the backup data center, the acquisition of equipment from the technology refreshment allowance, and a delay in the payment of contract award fees for the infrastructure services contract.

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

Fund Financial Results

($ in Millions)

Balance Sheet	Deposit Insurance Fund				
	Jun-18	Mar-18	Quarterly Change	Jun-17	Year-Over-Year Change
Cash and cash equivalents	$ 3,535	$ 3,119	$ 416	$ 3,362	$ 173
Investment in U.S. Treasury securities	88,300	84,831	3,469	75,043	13,257
Assessments receivable, net	2,679	2,783	(104)	2,677	2
Interest receivable on investments and other assets, net	558	581	(23)	399	159
Receivables from resolutions, net	3,711	5,194	(1,483)	8,944	(5,233)
Property and equipment, net	321	325	(4)	324	(3)
Total Assets	$ 99,104	$ 96,833	$ 2,271	$ 90,749	$ 8,355
Accounts payable and other liabilities	232	200	32	242	(10)
Liabilities due to resolutions	905	1,154	(249)	2,535	(1,630)
Postretirement benefit liability	259	259	-	232	27
Contingent liability for anticipated failures	85	113	(28)	117	(32)
Contingent liability for litigation losses and other	35	35	0	35	0
Total Liabilities	$ 1,516	$ 1,761	$ (245)	$ 3,161	$ (1,645)
FYI: Unrealized gain (loss) on U.S. Treasury securities, net	(1,137)	(975)	(162)	16	(1,153)
FYI: Unrealized postretirement benefit (loss) gain	(46)	(46)	-	(26)	(20)
Fund Balance	$ 97,588	$ 95,072	$ 2,516	$ 87,588	$ 10,000



During the first half of 2018, 25 securities matured totaling $12.6 billion (par value) with a weighted average yield of 1.18%. In this same period, 52 securities were purchased totaling $19.6 billion (par value) with a weighted average yield of 2.39%. The FDIC was able to benefit from the rising rate environment by purchasing higher yielding securities than those that had matured.

Fund Financial Results - continued

($ in Millions)

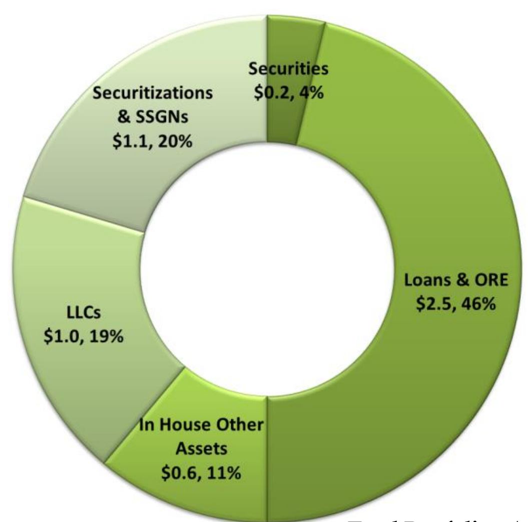
Income Statement (year-to-date)	Deposit Insurance Fund				
	Jun-18	Mar-18	Quarterly Change	Jun-17	Year-Over-Year Change
Assessments	$ 5,448	$ 2,850	$ 2,598	$ 5,371	$ 77
Interest on U.S. Treasury securities	719	338	381	478	241
Other revenue	5	1	4	6	(1)
Total Revenue	$ 6,172	$ 3,189	$ 2,983	$ 5,855	$ 317
Operating expenses	878	433	445	892	(14)
Provision for insurance losses	(206)	(65)	(141)	532	(738)
Insurance and other expenses	1	0	1	0	1
Total Expenses and Losses	$ 673	$ 368	$ 305	$ 1,424	$ (751)
Net Income	5,499	2,821	2,678	4,431	1,068
Unrealized gain (loss) on U.S. Treasury securities, net	(658)	(496)	(162)	(5)	(653)
Unrealized postretirement benefit gain (loss)	-	-	-	-	-
Comprehensive Income	$ 4,841	$ 2,325	$ 2,516	$ 4,426	$ 415

Selected Financial Data	FSLIC Resolution Fund				
	Jun-18	Mar-18	Quarterly Change	Jun-17	Year-Over-Year Change
Cash and cash equivalents	$ 892	$ 889	$ 3	$ 881	$ 11
Accumulated deficit	(124,597)	(124,601)	4	(124,607)	10
Total resolution equity	893	889	4	882	11
Total revenue	7	3	4	3	4
Operating expenses	0	0	0	0	0
Losses related to thrift resolutions	0	0	0	0	0
Net Income (Loss)	$ 7	$ 3	4	$ 3	4

Receivership Selected Statistics June 2018 vs. June 2017

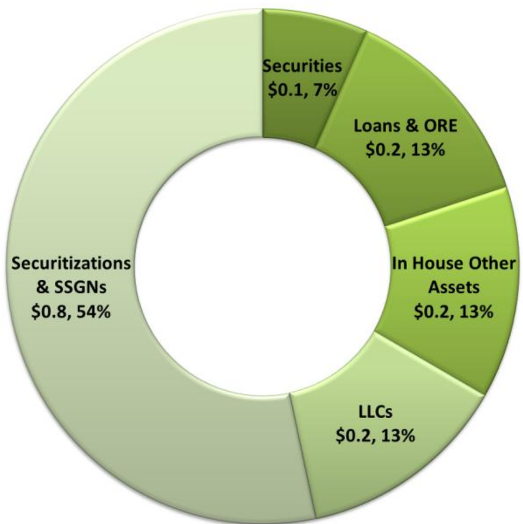
	DIF			FRF			ALL FUNDS		
($ in millions)	Jun-18	Jun-17	*Change*	Jun-18	Jun-17	*Change*	Jun-18	Jun-17	*Change*
Total Receiverships	302	372	(70)	0	0	-	302	372	(70)
Assets in Liquidation	$ 1,537	$ 5,421	$ (3,884)	$ 2	$ 2	$ -	$ 1,539	$ 5,423	$ (3,884)
YTD Collections	$ 993	$ 718	$ 275	$ -	$ -	$ -	$ 993	$ 718	$ 275
YTD Dividend/Other Pmts - Cash	$ 2,448	$ 1,402	$ 1,046	$ -	$ -	$ -	$ 2,448	$ 1,402	$ 1,046

Receivership Assets in Liquidation Balance at June 30, 2017 (in billions)



Total Portfolio = $5.4 billion

Receivership Assets in Liquidation Balance at June 30, 2018 (in billions)



Total Portfolio = $1.5 billion

Deposit Insurance Fund Portfolio Summary (Dollar Values in Millions)			
	6/30/18	12/31/17	Change
Par Value	$93,092	$85,376	$7,716
Amortized Cost	$93,079	$85,707	$7,372
Total Market Value (including accrued interest)	$92,344	$85,590	$6,754
Primary Reserve [1]	$92,344	$85,590	$6,754
Primary Reserve % of Total Portfolio	100.0%	100.0%	0.0%
Yield-to-Maturity [2]	1.78%	1.52%	0.26%
Weighted Average Maturity (in years)	1.94	2.05	-0.11
Effective Duration (in years)			
Total Portfolio	1.86	1.97	-0.11
Available-for-Sale Securities	1.97	2.07	-0.10
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)			
	6/30/18	12/31/17	Change
FRF-FSLIC			
Book Value [4]	$848	$842	$6
Yield-to-Maturity	1.78%	1.20%	0.58%
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)			
	6/30/18	12/31/17	Change
Book Value [5]	$3,501	$4,733	($1,232)
Effective Annual Yield	1.83%	1.24%	0.59%
Weighted Average Maturity (in days)	46	51	(5)

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

<table>
<tr><th colspan="2">Investment Strategies</th></tr>
<tr><td rowspan="3">DEPOSIT INSURANCE FUND</td><td>Strategy for the 2nd Quarter 2018
Purchase up to $15 billion (par value) of Treasury securities with maturity dates between September 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 $2 billion (par value) of newly purchased securities maturing between July 1, 2021, and June 30, 2023.</td></tr>
<tr><td>Strategy Changes for the 3rd Quarter 2018</td></tr>
<tr><td>Purchase up to <u>$13 billion</u> (par value) of Treasury securities with maturity dates between <u>December 31, 2018</u>, and <u>December 31, 2023</u>, 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 <u>January 1, 2022</u>, and <u>December 31, 2023</u>.</td></tr>
<tr><td rowspan="3">NATIONAL LIQUIDATION FUND</td><td>Strategy for the 2nd 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.</td></tr>
<tr><td>Strategy Changes for the 3rd Quarter 2018</td></tr>
<tr><td>No strategy changes for the third quarter of 2018.</td></tr>
</table>

Executive Summary of 2018 Budget and Expenditures by Budget Component and Major Expense Category Through June 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	$612,895	$594,671	97%	($18,224)
Outside Services - Personnel	257,909	122,994	108,570	88%	(14,424)
Travel	92,781	46,092	43,404	94%	(2,688)
Buildings	106,307	48,870	43,845	90%	(5,025)
Equipment	113,069	62,778	44,278	71%	(18,500)
Outside Services - Other	16,197	8,468	8,129	96%	(339)
Other Expenses	13,370	6,295	6,284	100%	(11)
Total Ongoing Operations	**$1,827,035**	**$908,392**	**$849,181**	**93%**	**($59,211)**
Receivership Funding					
Salaries & Compensation	$19,390	$10,862	$7,876	73%	($2,986)
Outside Services - Personnel	185,600	78,832	74,938	95%	(3,894)
Travel	3,574	1,776	998	56%	(778)
Buildings	6,968	3,482	2,542	73%	(940)
Equipment	969	463	271	59%	(192)
Outside Services - Other	1,327	669	507	76%	(162)
Other Expenses	7,172	3,582	1,804	50%	(1,778)
Total Receivership Funding	**$225,000**	**$99,666**	**$88,936**	**89%**	**($10,730)**
Office of Inspector General					
Salaries & Compensation	$34,853	$17,426	$15,998	92%	($1,428)
Outside Services - Personnel	1,660	830	819	99%	(11)
Travel	1,583	791	426	54%	(365)
Buildings	0	0	0		0
Equipment	1,555	778	88	11%	(690)
Outside Services - Other	0	0	0		0
Other Expenses	447	224	77	34%	(147)
Total Office of Inspector General	**$40,098**	**$20,049**	**$17,408**	**87%**	**($2,641)**
Total FDIC Operating Budget	**$2,092,133**	**$1,028,107**	**$955,525**	**93%**	**($72,582)**

Executive Summary of 2018 Budget and Expenditures by Division/Office Through June 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	$587,399	$291,807	$283,058	97%	($8,749)
Resolutions & Receiverships	237,492	118,484	110,529	93%	(7,955)
Administration	275,801	131,904	123,280	93%	(8,624)
Legal	200,239	100,531	95,152	95%	(5,379)
Information Technology	245,347	126,851	105,898	83%	(20,953)
Depositor & Consumer Protection	184,268	92,231	87,396	95%	(4,835)
Insurance & Research	51,711	25,748	25,137	98%	(611)
CIO Council	52,118	23,155	20,601	89%	(2,554)
Finance	40,812	20,260	19,851	98%	(409)
Inspector General	40,098	20,049	17,408	87%	(2,641)
Chief Information Security Officer	51,235	25,818	20,521	79%	(5,297)
Executive Support [1]	22,580	10,707	10,089	94%	(618)
Complex Financial Institutions	19,767	9,223	9,053	98%	(170)
Corporate University - Corporate	26,744	16,265	13,481	83%	(2,784)
Corporate University - CEP	19,054	9,336	9,073	97%	(263)
Executive Offices [2]	11,073	5,738	4,998	87%	(740)
Corporate Unassigned	26,395	0	0		0
Total FDIC Operating Budget	**$2,092,133**	**$1,028,107**	**$955,525**	**93%**	**($72,582)**

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.