MESSAGE FROM THE CHAIRMAN

For 84 years, the FDIC has carried out its mission of maintaining public confidence and stability in the U.S. financial system. The FDIC does this by insuring deposits; supervising and examining financial institutions for safety, soundness, and consumer protection; making large firms resolvable; and managing receiverships when banks fail.

At the end of September 2017, the FDIC insured deposits of $7.1 trillion in more than 580 million accounts at 5,738 institutions, supervised 3,669 institutions, and managed 367 active receiverships with total assets of nearly $5 billion.

The year 2018 marks a full decade since the start of the financial crisis. Stemming the crisis required unprecedented actions by the U.S. government, including the FDIC, to restore confidence in financial markets and to address the problems of systemically important financial institutions. The FDIC recently published a history, *Crisis and Response: An FDIC History 2008–2013,* to document the lessons learned during that period. The study is intended to serve as a guidepost for future policymakers who will someday be called upon to respond to the next period of financial instability.

One of the most important lessons the book conveys—for regulators and bankers alike—is that we must not become complacent when economic and banking conditions appear strong. It is precisely during these times that the seeds can be sown for the next financial crisis.

History shows that surprising and adverse developments in financial markets occur with some frequency. History also shows that the seeds of banking crises are sown by the decisions banks and bank policymakers make when they have maximum confidence that the horizon is clear. It is also worth keeping in mind that the evolution of the global financial system toward greater interconnectedness and complexity may tend to increase the frequency, severity, and speed with which financial crises occur. It would be a mistake to assume a severe downturn or crisis cannot happen again.

Over the past decade, the banking system has transitioned from a position of extreme vulnerability to a position of strength. Operating with the stronger cushions of capital and liquidity required by the post-crisis reforms, U.S. banking organizations are experiencing strong earnings growth and are providing support to the U.S. economy.

The challenge for the FDIC going forward will be to preserve the hard-earned improvements in the capital and liquidity of U.S. banking institutions and to sustain vigilant supervision of the banking industry, both to continue the strong performance of banks during this post-crisis period and to position the banking system to weather the next, inevitable downturn.

Following is an overview of the current economic and financial outlook, the FDIC's important accomplishments over the past year, as well as the strategic challenges we face.

THE CURRENT OUTLOOK

After experiencing the most severe financial crisis and economic downturn since the 1930s in 2008–2009, the U.S. economy is now well into its ninth year of recovery. Growth in real gross domestic product

(GDP) has averaged 2.2 percent in this expansion, and was right around 3 percent in the second and third quarters of 2017. The stock market has reached new highs and real estate prices have been rising. Global economic growth appears to be picking up, with the International Monetary Fund raising its growth forecasts for Japan, China, and Europe.

This post-crisis economic expansion is the third-longest expansion in U.S. history. In June 2018 it would become the second-longest expansion in our history. Banks have been able to use this period to rebuild their balance sheets and strengthen capital and liquidity. They have achieved steady growth in net income and loan balances and improved credit quality.

In 2017 the industry saw a gradual slowdown in the annual rate of loan growth, which appears to be a function of the demand for credit rather than the supply. During the 12 months ended September 30, loan balances at banks increased by $322 billion, down from a $466 billion increase in 2016. Loan growth was strongest at community banks, which posted a 7.3 percent gain versus 3.5 percent for the industry overall.

This improvement in the economic outlook is a positive development for banks and bank regulators. We know, however, that economic expansions eventually come to an end. We also know that financial shocks can come from unexpected sources at any time.

Following the Savings & Loan crisis of the 1980s and the banking crisis of the late 1980s and early 1990s, we entered a 10-year economic expansion—the longest in U.S. history. Even that period was punctuated by a series of domestic and international crises that tested the effectiveness of risk managers. Banking and economic crises emerged during the 1990s and into the early 2000s in Scandinavia, Mexico, east Asia, Russia, and Argentina. Domestically, severe disruptions were averted in 1998 following the collapse of Long-Term Capital Management that resulted from its use of high-risk arbitrage trading strategies. The 2001 crash in dot-com equity prices was soon followed by the sudden bankruptcies of Enron and WorldCom. Finally, the development that would ultimately trigger the recent financial crisis was the decision by financial institutions in increasing numbers, and of increasing size, to enter the business of originating or securitizing subprime and alternative mortgages.

Such experience is a reminder that, despite the good conditions we currently see, there are always challenges that could quickly change the outlook. Even though the current expansion appears more sustainable than the boom that occurred in the years leading up to the 2008 crisis, there are vulnerabilities in the system that merit our attention.

One vulnerability relates to the uncertainties associated with the transition of monetary policies—both here and abroad—from a highly expansionary to a more normal posture. Market responses to changes in monetary policy can be hard to predict. Recently, the Board of Governors of the Federal Reserve System has embarked on a gradual reduction in the size of its balance sheet. Thus far, there has been no apparent market reaction. Nonetheless, higher interest rates could pose problems for industry sectors that have become more indebted during this expansion.

By many measures, stocks, bonds, and real estate are richly priced. Stock price-to-earnings ratios are at high levels, traditionally a cautionary sign to investors of a potential market correction. Bond maturities have lengthened, making their values more sensitive to a change in interest rates. As measured by capitalization rates, prices for commercial real estate are at high levels relative to the revenues the properties generate, again suggesting greater vulnerability to a correction.

Taken together, these circumstances may represent a significant risk for financial market participants. While the banking system is much stronger now than it was entering the crisis, continued vigilance is warranted.

FOCUSING ON INTEREST-RATE RISK, CREDIT RISK, AND LIQUIDITY RISK

While the financial performance of the banking industry continues to improve, evidence of growing interest-rate risk, credit risk, and liquidity risk merit attention. A prolonged period of low interest rates has resulted in narrow net interest margins, and many banks have responded by investing in longer-term assets, which has increased the mismatch between asset and liability maturities.

Examiners have also noted that lending in higher-risk loan categories has been increasing, and that institutions with concentrated portfolios have been growing more rapidly and placing greater reliance on potentially volatile funding sources than the rest of the industry. The FDIC will continue to monitor these trends, as well as the risk-management practices of supervised institutions associated with loan underwriting, credit administration, and portfolio management.

In 2016, the FDIC, Federal Reserve Board, and Office of the Comptroller of the Currency (OCC) increased the frequency of examinations of large banks that participate in the Shared National Credit (SNC) program. The most recent report, which reflects examinations conducted in the third quarter of 2016 and first quarter of 2017, noted that credit risk in the portfolio remains elevated due to borrowers that exhibited excessive leverage, as well as distressed loans in the oil and gas sector.

During 2017, the FDIC observed instances of liquidity stress at a small number of insured financial institutions and broad trends of reduced balance sheet liquidity among smaller banks. In response, the FDIC co-hosted an interagency community bank teleconference to discuss trends in community bank liquidity and funds management and the importance of sound risk-management practices. The FDIC, Federal Reserve Board, OCC, and Conference of State Bank Supervisors reiterated the importance of a strong cushion of liquid assets and diversified funding, and discussed brokered deposit restrictions, cash flow scenario analysis and sensitivity testing, and contingency funding planning.

Further, in conjunction with the Federal Reserve Board and OCC, we issued a series of frequently asked questions to address the applicability of the liquidity coverage ratio rule, which was adopted in 2014 to implement a quantitative liquidity requirement consistent with the standard established by the Basel Committee on Banking Supervision.

These examples of increasing risk are noteworthy because it is during this phase of the credit cycle that underwriting and investment decisions are made that may lead to losses in the future. Addressing these risks before losses materialize will benefit banks and contribute to the stability and resilience of the industry. We will continue to focus our supervisory attention on these risk areas going forward.

ADDRESSING CYBERSECURITY RISK

The rapidly evolving nature of cybersecurity risk reinforces the need for regulators, financial institutions, and critical technology service providers to have high-quality controls and clear and tested business continuity plans. The FDIC collaborates with other financial regulators, law enforcement, security agencies, and public-private partnerships to better understand the cybersecurity threats to the financial system, and to identify opportunities to adjust supervisory strategies to increase their effectiveness.

The FDIC, Federal Reserve Board, and OCC continue to collaborate to strengthen cybersecurity risk management among the entities we supervise. For example, in 2017, we updated the interagency Cybersecurity Assessment Tool that helps financial institutions determine their cyber risk profile, inherent risks, and level of cybersecurity preparedness. This update addressed feedback from entities that are using the tool.

The FDIC monitors cybersecurity issues on a regular basis through on-site bank examinations. In 2016, we introduced the Information Technology Risk Examination Program to enhance our ability to identify, assess, and validate information technology and operations risks in financial institutions. We are using information gathered through the program to provide more specific, targeted findings with respect to information technology, which can help financial institutions better prioritize their actions.

The FDIC, Federal Reserve Board, and OCC jointly examine the services multiple companies provide to the banking industry. We introduced a new cybersecurity examination work program in 2017 that has improved our risk focus on cybersecurity, among other information technology risks. Additionally, in December, we held a roundtable meeting with some of the most significant service providers to discuss key risk topics, including cybersecurity.

In 2017, the FDIC also continued to strengthen its own cybersecurity posture. Our Insider Threat and Counterintelligence Program is in place to safeguard employees, information, operations, and facilities, and we continue to enhance our procedures and programs for securing sensitive information. The FDIC also requires employees to take annual security and privacy training so they are aware of our security standards. This is supplemented by periodic exercises to help ensure employees stay alert to possible outside threats.

Information security is a top priority at the FDIC. We will continue to enhance our security controls in light of the changing threat landscape.

RESOLUTION OF SYSTEMICALLY IMPORTANT FINANCIAL INSTITUTIONS

The FDIC continues to evaluate firm-developed resolutions plans, and to develop its own strategies to facilitate the orderly failure of large, complex, Systemically Important Financial Institutions (SIFIs) without taxpayer support or market breakdowns.

Living Wills

In 2017, the FDIC remained committed to carrying out the statutory mandate that SIFIs demonstrate a clear path to an orderly failure under bankruptcy at no cost to taxpayers. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, bankruptcy is the statutory first option for resolving a SIFI. To satisfy this requirement, the largest bank holding companies and certain non-bank financial companies are required to prepare resolution plans, also referred to as "living wills." These living wills must demonstrate that the firm could be resolved under bankruptcy in a rapid and orderly manner that substantially mitigates the risk that its failure would have serious adverse effects on financial stability in the United States.

The FDIC and the Federal Reserve Board are charged with jointly reviewing and assessing each firm's resolution plan. The eight largest U.S. systemically important banking organizations submitted their plans by July 2017. In December, the FDIC and Federal Reserve Board completed their review. We identified no deficiencies, but did identify shortcomings in the plans of four firms. While the agencies agreed these weaknesses did not necessitate immediate plan resubmissions, they are important enough to highlight and have addressed in the firms' next plan submissions, which are required by July 1, 2019.

These results represent the significant progress firms have made to modify their corporate structures so that losses can be borne by investors in an orderly way. However, inherent challenges and uncertainties associated with the resolution of a SIFI remain. Toward that end, the agencies identified four areas in which more work needs to be done by all firms to continue to improve their resolvability: intra-group liquidity; internal loss-absorbing capacity; derivatives; and payment, clearing, and settlement activities.

Moreover, the resolvability of firms will change as markets change and as firms' activities, structures, and risk profiles change. We expect the firms to remain vigilant in considering the resolution consequences of their day-to-day management decisions.

In addition to the eight U.S. firms, in March 2017 the agencies issued guidance to four foreign banking organizations to help them improve their resolution plans and to reflect the significant restructuring that they have undertaken to form intermediate holding companies within the United States. The feedback was organized around a number of key vulnerabilities, such as capital, liquidity, and corporate governance mechanisms. These four firms will file their next plans in 2018.

Overall, the living will process has proved to be an important means for identifying and implementing measures to enhance SIFIs' resolvability. Firms have taken significant actions, including restructurings, operational continuity planning, and options for separating assets, business lines, and entities from a failing company. Firms also have improved their management information systems capabilities, financial resource measurement and processes, and resolution planning governance, all of which are key elements for enhancing resolvability.

The FDIC and Federal Reserve Board are exploring ways to further improve the resolution planning process. One measure we are considering is extending the cycle for living will submissions to every two years and focusing, on an alternating basis, on key topics and material changes from the prior full plan. In addition, there may be opportunities to reduce the submission requirements for a large number of firms due to their relatively small, simple, and domestically focused banking activities.

Orderly Liquidation Authority

Given the challenges and uncertainty surrounding any particular failure, Title II of the Dodd-Frank Act provides the Orderly Liquidation Authority for circumstances when an orderly failure in bankruptcy might not be possible. This authority allows the FDIC to manage the orderly failure of a firm when failure in bankruptcy might threaten financial stability.

Coupled with the Federal Reserve's Total Loss-Absorbing Capacity (TLAC) rule, which requires a minimum amount of long-term unsecured debt that can be converted to equity in resolution, these authorities work together to increase the likelihood that financial markets and the broader economy can weather the failure of a SIFI; that shareholders, creditors, and culpable management of the institution will be held accountable without cost to taxpayers; and that such an institution can be wound down and liquidated in an orderly way.

As has occurred in the United States, the other leading jurisdictions of the world have enacted expanded authorities for the resolution of SIFIs. The FDIC has worked closely with all major financial jurisdictions, including the United Kingdom, the European Banking Union, Switzerland, and Japan, to facilitate cross-border resolution planning.

In the years since enactment of Dodd-Frank, the FDIC has made significant progress in developing the operational capabilities necessary to carry out a resolution under the Orderly Liquidation Authority if needed. The fact that the credit rating agencies have lowered the credit ratings of the eight U.S. Global Systemically Important Banks (G-SIBs) because of a reduced expectation of taxpayer support in the event of failure is a sign of that progress.

Until we actually execute a resolution using these authorities we should be cautious about bold statements. However, we have a domestic and international framework in place today that would have been extremely helpful in 2008, and that should promote a better outcome in the future.

REBUILDING THE DIF, RESOLVING FAILED BANKS

Under a restoration plan that reflects the statutory requirement to rebuild the Deposit Insurance Fund (DIF), the fund balance has increased every quarter since the end of 2009, when it reached an all-time low. As of December 31, 2017, the fund balance had increased to $92.7 billion. The DIF reserve ratio—the ratio of the DIF balance to estimated insured deposits—was 1.28 percent at September 30, 2017, the highest reserve ratio since June 2005.

The Dodd-Frank Act raised the minimum reserve ratio for the DIF from 1.15 percent to 1.35 percent, and mandates that the reserve ratio reach 1.35 percent by September 30, 2020. Dodd-Frank also assigns the cost of that increase in the minimum reserve ratio to banks with $10 billion or more in total assets.

To meet these requirements, large banks have been paying temporary assessment surcharges. Surcharges began in the third quarter of 2016—the quarter after the reserve ratio surpassed 1.15 percent—and will continue through the quarter in which the reserve ratio first meets or exceeds 1.35 percent. The FDIC expects the reserve ratio to reach 1.35 percent in 2018, ahead of the September 2020 statutory deadline.

In the event that the reserve ratio does not reach 1.35 percent by the end of 2018, FDIC regulations call for a shortfall assessment in early 2019 on banks with total assets of $10 billion or more to cover the gap.

In 2017, the numbers of failed banks and problem banks continued their trend toward pre-crisis levels. There were eight bank failures in 2017, down dramatically from a yearly peak of 157 in 2010, while the number of banks on the problem bank list (banks rated 4 or 5 on the CAMELS rating scale) fell to 104 at the end of September 2017 from a high of 888 in March 2011.

During 2017, the FDIC successfully used various resolution strategies to protect insured depositors of failed institutions at the least cost to the DIF. The FDIC actively marketed failing institutions and sold them to other financial institutions. These strategies protected insured depositors and preserved banking relationships in many communities, providing depositors and customers with uninterrupted access to essential banking services.

MANAGING FDIC RESOURCES

As the banking industry continues to recover, the FDIC requires fewer resources. The agency's authorized workforce for 2017 was 6,363 full-time equivalent positions compared with 6,533 the year before. The 2017 FDIC Operating Budget was $2.16 billion, a decrease of 2.4 percent from 2016.

The FDIC remains committed to fulfilling its mission while prudently managing costs. We reduced our budget for 2018 from the prior year by 3.0 percent to $2.09 billion and reduced authorized staffing by approximately 4.5 percent to 6,076 positions. This is the eighth consecutive reduction in the FDIC's annual operating budget. However, contingent resources are included in the budget to ensure readiness should economic conditions unexpectedly deteriorate.

COMMUNITY BANKING INITIATIVE

The FDIC is the primary federal supervisor of the majority of community banks in the United States, and community banks account for 92 percent of FDIC-insured institutions. For these reasons, community banking is an important focus of FDIC supervision, technical assistance, and research. The FDIC maintains an extensive community bank research program, hosts community banking conferences, and convenes an Advisory Committee on Community Banking, through which the FDIC Board receives regular input from bankers.

Community banks are critically important to our economy and the banking system. Community banks account for 13 percent of the banking assets in the United States, and 43 percent of the small loans to businesses and farms originated by all banks, making them key partners in supporting local economic development and job creation. The community banking sector continues to demonstrate resilience and innovation in meeting new challenges and competing in an evolving financial marketplace.

Helping community banks meet the challenges they face is an important part of the FDIC's Community Banking Initiative. These include challenges in the areas of recruitment and succession planning. In response, the FDIC developed a directory of universities and colleges that have established academic programs dedicated to community banking, and is working with the American Bankers Association to explore the feasibility of establishing an online clearinghouse through which banks can connect with universities and colleges seeking to place students who have an interest in banking internships and jobs.

Also in 2017, in response to feedback from our Advisory Committee on Community Banking, we prepared a virtual version of the Directors' Colleges that we deliver throughout our regions. The virtual curriculum includes six video modules covering topics directors most often tell us they want to learn more about: interest-rate risk, troubled debt restructurings, the Bank Secrecy Act, and corporate governance.

The FDIC also hosted banker webinars focusing on financial education, accessing affordable mortgage credit, and changes to the Call Report. Additionally, we conducted 11 banker teleconferences to discuss changes to the Home Mortgage Disclosure Act, proposed changes to the capital rules, small business resources for community banks, liquidity and funds management, the Bank Secrecy Act, Community Development Lending, reasonably expected market areas, and new accounting proposals.

In addition, we conducted three seminars on FDIC deposit insurance coverage for bank officers and employees, and released three videos covering Fundamentals of Deposit Insurance Coverage, Deposit Insurance Coverage for Revocable Trust Accounts, and Advanced Topics in Deposit Insurance Coverage.

The FDIC also published a new guide to help community bankers learn more about the programs and products offered by the Federal Home Loan Banks (FHLBs) to facilitate mortgage lending. The first two parts of the Guide focus on *Federal Agencies and Government-Sponsored Enterprises* and *State Housing Finance Agencies*. The *Affordable Mortgage Lending Guide, Part III: Federal Home Loan Banks* describes many of the products and services offered by FHLBs, including products that support single-family home purchases, and alternatives for selling mortgages on the secondary market. The three-part guide is available through the FDIC's Affordable Mortgage Lending Center, an online resource to help community bankers understand and compare the mortgage-lending products and services offered by federal and state housing finance agencies, the FHLBs, and government-sponsored enterprises.

In 2016 the FDIC launched a new survey regarding banks' small business lending practices. This survey was designed to solicit and report information on the general characteristics of banks' small business borrowers, the types of credit offered to small businesses, and the relative importance of commercial lending for banks of different sizes and business models. This information increases the understanding of how banks of all sizes are lending to small businesses, which is crucial to job creation. The survey has generated valuable data about a previously under-researched area, and a full report of the survey results will be released in 2018.

Finally, the FDIC's Advisory Committee on Community Banking is an ongoing forum for discussing current issues and receiving valuable feedback from the industry. The committee, which met three times during 2017, is composed of chief executives of 13 community banks located around the country. The committee provides valuable input on a wide variety of topics, including examination policies and procedures, capital and other supervisory issues, credit and lending practices, deposit insurance assessments and coverage, and regulatory compliance issues.

Supporting *De Novo* Banks

De novo institutions fill important gaps in local banking markets, provide credit and services to communities that may be overlooked by larger institutions, and help to preserve the vitality of the community banking sector. The FDIC is committed to working with, and providing support to, any group with an interest in starting a *de novo* bank, and welcomes applications for deposit insurance.

The current environment, with low interest rates and the resulting impact on net interest margins, is challenging for the formation of new banks. Nevertheless, we have seen tentative signs of an uptick in *de novo* formations, including increased interest from prospective organizing groups in filing applications for new insured depository institutions. During 2017, the FDIC approved six applications for deposit insurance for new community banks.

To encourage interest and help organizing groups navigate the application process, the FDIC conducted a series of outreach meetings throughout the country. These meetings aimed to help organizing groups become fully informed about the FDIC's application process and the tools and resources available to assist them. We also issued a publication entitled *Applying for Deposit Insurance – A Handbook for Organizers of De Novo Institutions* that is intended to help organizers become familiar with the deposit insurance application process and understand the path to obtaining insurance.

SIMPLIFYING REGULATION

In March of 2017, the FDIC, OCC and Federal Reserve Board (FRB) in conjunction with the National Credit Union Administration (NCUA), all members of the Federal Financial Institutions Examination Council (FFIEC), issued a joint report to Congress detailing our extensive, two-year review of the rules affecting financial institutions. This review is required by the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), and its purpose is to identify and eliminate, as appropriate, outdated or otherwise unnecessary regulatory requirements on insured depository institutions, while, at the same time, ensuring that safety and soundness and consumer compliance standards are maintained.

The EGRPRA-mandated review is required at least once every 10 years, and this review cycle included, for the first time, the significant body of new rules and regulations introduced in response to the financial crisis.

The regulatory review process is one we take very seriously. Over the course of the review, the federal banking agencies and the NCUA hosted six public outreach meetings and reviewed more than 230 comment letters submitted in response to four *Federal Register* notices. The agencies have reviewed these comments and considered appropriate changes to reduce regulatory burdens on institutions. We also explored opportunities to improve the transparency and clarity of our supervisory policies and procedures, especially as they apply to community banks.

Together with the other FFIEC agencies, we have taken certain steps and continue to take further measures to address the significant issues identified as burdensome by supervised institutions during the EGRPRA review process. For example:

- We adopted a final rule that expanded the examination cycle for certain insured depository institutions with up to $1 billion in total assets. Approximately 4,790 insured depository institutions are now eligible for the expanded exam cycle.
- We streamlined the Call Report, removing 40 percent of the data items previously required for institutions with domestic offices only and reducing the length of the Call Report for eligible small institutions from 85 pages to 61 pages. In June 2017, and again in November 2017, we proposed additional burden-reducing revisions to all three versions of the Call Report.
- We issued an interagency proposal to simplify the generally applicable capital framework and to clarify the definition of high-volatility commercial real estate. The proposed simplifications include changes to the regulatory capital treatment of mortgage servicing assets, deferred tax assets, investments in the capital instruments of other financial institutions, and minority interest.
- We finalized a rule regarding regulatory capital to pause the phase-in of certain regulatory capital adjustments and deductions that are part of the Basel III capital standard.
- We issued an interagency proposal to increase the threshold for requiring an appraisal on commercial real estate loans, which we believe will reduce regulatory burden in a manner consistent with safety and soundness. Comments

on the proposal have been received and are being evaluated.

- We issued an interagency bulletin to make bankers and other stakeholders aware of the options available in areas where there is a shortage of appraisers. The advisory addresses concerns raised pursuant to the EGRPRA review process, as well as during six roundtables between federal banking regulators, state commissioners, and rural community bankers.
- We raised the threshold for loans included in the SNC program from $20 million to $100 million. This action lowered the number of loans required to be reported by financial institutions, providing regulatory relief for 82 mid-sized financial institutions.

The federal banking agencies also recognize that regulatory burden does not emanate solely from statutes and regulations, but often comes from processes and procedures related to examinations and supervisory oversight. Accordingly, the agencies are jointly reviewing the examination process, examination report format, and examination report preparation process. We are working to identify opportunities to minimize burden to bank management where possible, with a particular goal of determining whether technology can be used to make existing examination activities more efficient or allow for additional safety and soundness examination work to be conducted off-site.

EGRPRA commenters recommended a number of legislative changes as well, and the FDIC is supportive of reforms that would:

- Raise the total assets threshold for conducting annual stress tests from $10 billion to $50 billion;
- Increase the asset threshold for banks eligible for an 18-month examination cycle from $1 billion to $2 billion;
- Raise the asset threshold for the community bank Call Report to match a higher examination frequency threshold;
- Create a new appraisal threshold exemption for insured depository institutions that originate a *de minimis* number (i.e., less than 25) of residential mortgage loans in a calendar year; and
- Deem banks with assets under $10 billion compliant with risk-based capital requirements if they maintain a leverage capital ratio of 10 percent and do not engage in a short, specified list of activities.

Overall, the FDIC supports measures to ensure that financial regulations are simple and straightforward and that regulatory costs and burdens are minimized, particularly for smaller institutions. However, in considering ways to simplify or streamline regulations, it is important to preserve the gains that have been achieved in restoring confidence and stability since the financial crisis and maintaining the safety and soundness of the U.S. banking system.

REGULATORY RELIEF IN DISASTER AREAS

In 2017, communities in Florida, Georgia, Texas, and, in particular, the U.S. Virgin Islands and Puerto Rico, were affected by severe storms and flooding related to hurricanes. The FDIC worked to provide flexibility to financial institutions in these areas relative to appraisal requirements, lending and credit policies, and efforts to meet customers' cash and financial needs. As these areas continue to recover, the FDIC encourages depository institutions to consider all reasonable and prudent steps to assist their customers, consistent with safe-and-sound banking practices.

EXPANDING ACCESS TO BANKING SERVICES AND PROTECTING CONSUMERS

Expanding access to mainstream banking services helps strengthen confidence in the nation's financial system, the FDIC's core mission. Our most recent National Survey of Unbanked and Underbanked Households, published in October 2016, produced encouraging results, showing that the proportion of unbanked households has fallen to 7 percent. But the survey provides ample evidence that much work remains to expand economic inclusion, particularly among households with incomes below $30,000 per year, African American households, Hispanic households, and households headed by a working-age individual with a disability.

Building on the insights gained from the survey, the FDIC has undertaken a number of initiatives to expand economic inclusion.

The FDIC introduced the Safe Accounts pilot in 2011 in response to survey findings and with the encouragement of the Advisory Committee on Economic Inclusion. Safe Accounts have a low or no minimum balance requirement, are electronic-based, use debit cards, do not include overdraft or nonsufficient funds fees, and have low, transparent monthly fees. These accounts are designed to better enable unbanked and underbanked households to access the banking system and to sustain banking relationships over time.

Since the pilot concluded, we have identified examples of banks across the spectrum of the industry—money center, regional, and community banks— as offering accounts consistent with the features of the Safe Account. FDIC analysts estimate that nine in 10 Americans live in a county with a branch of an institution that offers Safe Accounts. This represents a significant improvement since 2011, but many banks and consumers remain unaware of the benefits of these low-cost, card-based products. To ensure that consumers who would benefit from Safe Accounts are aware of their availability and to encourage bank engagement, the FDIC has partnered with the non-profit Cities for Financial Empowerment Fund, *Bank On* programs, and FDIC-supported Alliances for Economic Inclusion, and has worked with other community groups, banks, state and local governments, and philanthropic organizations. Through these forums, we provide outreach to representatives of hundreds of community-based organizations and bankers across the country. Bringing these groups together creates opportunities to identify strategies to reach unbanked populations by lowering the barriers to accessing banking services.

In addition to the Safe Account effort, the FDIC continues to study how mobile financial services may help banks address many of the core financial service needs of underserved consumers, including providing more timely information about balances and transactions and more control over customers' financial lives.

We also continued our efforts to provide and promote effective financial education for young people. Offering financial education to school-age children opens the door to many opportunities and establishes the groundwork for a lifelong banking relationship. Through our Youth Savings Pilot program, we have studied the financial education programs offered by 21 banks in partnership with local schools over a two-year period. These programs tie financial education with the opportunity to open a safe, low-cost savings account at bank branches, some of which are located in the schools and run by students.

We gathered insights from the pilot into a report we published in March 2017. The many lessons we learned—about program design, the importance of partnerships, types of accounts offered, classroom-based financial education, the role of parents and guardians, program costs, and measuring performance—provide a comprehensive roadmap for banks and schools that are teaming up to link financial education with opportunities to save.

The FDIC also launched a Youth Banking Network, a platform to support banks as they work with school and nonprofit partners to create and expand youth savings programs. The FDIC offers periodic conference calls and resources on topics of interest to network members, which now total more than 50 institutions, and receives ongoing feedback from network participants on ways to support collaborations.

Our *Money Smart* program is another example of our ongoing efforts to develop and promote financial education. For example, *Money Smart for Older Adults*, a resource developed jointly by the FDIC and the Consumer Financial Protection Bureau, was updated in 2017 to help older adults and their caregivers guard against financial exploitation and make informed financial decisions.

We also continue to collaborate with the U.S. Small Business Administration (SBA) on *Money Smart for Small Business*, a resource that provides practical guidance for starting and managing a business. The Strategic Alliance Memorandum between the FDIC and SBA ensures this collaboration will continue through 2018.

Money Smart for Young People, a curriculum that involves educators, parents/caregivers, and young people in the learning process, continues to be well received. There have been more than 145,000 downloads of the curriculum, portions of which are available in Spanish, since its launch in 2015. These resources are at work in classrooms and also are used by workforce development organizations in providing financial education to young people in employment programs.

Many of these initiatives, as well as the future of economic inclusion efforts, were discussed at the Economic Inclusion Summit the FDIC hosted in April. The event brought together representatives from banks, trade associations, non-profit organizations, government agencies, and the public to explore strategies for increasing underserved consumers' access to the mainstream financial system. In particular, panelists discussed strategies for

- Establishing safe and sustainable banking relationships,
- Leveraging partnerships for banking access and financial empowerment, and
- Growing customer relationships and building long-term loyalty among diverse customers.

The FDIC's Advisory Committee on Economic Inclusion also met twice in 2017 to discuss topics such as neighborhood access to bank branches, economic inclusion for persons with disabilities, and an FDIC survey of entry-level consumer checking and savings accounts, as well as collaborations with community-based organizations and resources for affordable mortgage lending.

Overall, the progress the FDIC and our collaborators have made in this area has been substantial—initiating the national survey, developing the model Safe Account and seeing it offered by financial institutions around the country, and exploring the potential of mobile financial services to expand access.

CONCLUSION

During 2017, the U.S. banking industry continued its recovery from the recent financial crisis. The industry benefited from stronger balance sheets, fewer problem banks and bank closings, increased lending activity, and a larger balance in the DIF.

In 2018, the FDIC will continue to work to fulfill its mission of maintaining public confidence and stability in the nation's financial system.

As I previously emphasized, bankers and supervisors should not allow the current strong economic and banking conditions to be a cause for complacency.

The challenge for the FDIC going forward will be to preserve the hard-earned improvements in the capital and liquidity of U.S. banking institutions and sustain vigilant supervision of the banking industry, both to continue the strong performance of banks during this post-crisis period and to position the banking system to weather the next inevitable downturn.

The workforce of the FDIC remains committed to the agency's mission. I am very grateful to the dedicated professionals of the FDIC for their commitment to public service and for the high level at which they carry out their important responsibilities.

Sincerely,

Martin J. Gruenberg

Martin J. Gruenberg