Remarks

By

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Introduction

Good morning. It is an honor to be with you today to share my perspective on the state of banking and to discuss my priorities as the Comptroller of the Currency of the United States. It is great to be back in Tokyo, where I visited during my days as a banker with MUFG Union Bank. I am very grateful for the many opportunities I had to interact and learn from my experiences with Japanese bankers and business people over the years. As Comptroller of the Currency, I have gained a greater appreciation for the close ties between the United States and Japan that have developed over the last 70 years. Our countries trade nearly $300 billion in goods and services each year. We also have deep investment in each other's success with the United States investing more the $129 billion in Japanese stock in 2017 and Japan investing nearly $470 billion in the United States. Japan is one of the world's most successful democracies and largest economies. The U.S.-Japan Alliance is the cornerstone of U.S. security interests in Asia and is fundamental to regional stability and prosperity. I am honored to continue that relationship today.

As Comptroller of the Currency, I oversee 4,000 men and women who supervise more than 1,300 national banks, federal savings associations, and federal branches of foreign banks operating in the United States. These banks include the largest, most complex, and internationally active U.S. banks—such as JPMorgan Chase, Citibank, and Bank of America—as well as more than 1,200 smaller community banks that meet the needs of local consumers, businesses, and communities throughout the nation. Among these banks are federal branches of foreign banks operating in the United States, including multiple branches of Japanese banks. Combined, these banks hold nearly $12 trillion in assets and manage another $51 trillion in fiduciary and custody assets. These banks play an important role in the global economy—promoting growth, creating jobs, and providing economic opportunity.

The responsibility of my team at the Office of the Comptroller of the Currency (or OCC) is to ensure that the federal banking system in the United States operates in a safe and sound manner, provides fair access to financial services, treats customers fairly, and complies with laws and regulations. The men and women of the agency are proud to serve this important mission.

As I deliver these remarks, I am nearing the end of my first year as Comptroller. While that year provides me a unique perspective, my short time as Comptroller has also been informed by my long career as a banker. In fact, I am the first banker to be appointed Comptroller in more than 40 years. Being a banker provides me a strong foundation to build upon because I know first-hand the challenges that bankers face, the common mistakes that banks can make, and the opportunities they have to promote more economic growth.

Based on my experience as a banker, I arrived at the OCC last November with a focus on promoting economic opportunity and creating jobs. In my view the safeguards put in place after the financial crisis had succeeded. It was time to reassess our regulatory approach and carefully determine what we could do to reduce unnecessary burden on banks so that they could be the engines of economic opportunity they were meant to be. Creating economic growth and opportunity is at the core of a banker's identity. Bankers, in ways, make dreams come true, helping others achieve things they could never accomplish on their own. As Comptroller, I want bankers to help customers realize their dreams by reducing the unnecessary burden and inefficient regulation.

To that end, I want to share with you my perspective on the condition of banking in the United States and then discuss some of the things we are working on at the OCC that I believe can help banks fulfill their customers' dreams.

Condition of Banks in the United States

I am pleased to report that the condition of banks operating in the United States is strong. The system has rebounded from the crisis. Capital and liquidity are near historic highs. Bankers have a better understanding of the banks' risks than at any point in my 35-year banking career. Capital-to-total-assets ratio globally hovers around 10.3 percent, and in the United States, that ratio approaches almost 12 percent.[1] In the most recent stress tests on the largest commercial banks in the United States, the Federal Reserve concluded that all of the participating banks had capital sufficient to withstand a severe downturn in the economy.[2] Return on equity and asset quality are approaching pre-crisis levels. Bank profitability improved in 2017 and 2018 when compared with the previous year on a *pre-tax* basis. Pre-tax income rose 4 percent in 2017 for the federal banking system overall. Profitability in 2017 was limited in part because of tax changes affecting banks in the United States.

[1] See "Bank Capital to Asset Ratio." The World Bank (https://data.worldbank.org/indicator/FB.BNK.CAPA.ZS?view=chart).
[2] See "Federal Reserve Board Releases Results of Supervisory Bank Stress Tests." The Board of Governors of the Federal Reserve. June 21, 2018 (https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180621a.htm).

That improvement continues this year, and the economic environment is expected to continue to support loan growth and bank profitability through 2019. Credit quality, which is an important indicator of bank health, is good and generally has returned to normal pre-crisis levels. Return on assets among U.S. banks is projected to grow from 1.04 percent in 2016 to 1.25 percent in 2019.[3] U.S. gross domestic product (GDP) is forecast to continue its nine-year expansion through 2019. In the second quarter of 2018, U.S. GDP jumped 4.1 percent.[4] In the United States, we are nearing full employment with the unemployment rate falling to 3.9 percent in July 2018.[5] Those are positive indicators for the U.S. economy, which has such a large influence globally.

Risks Facing Banks

Still, bankers know that the worst loans are made in the best of times, and we must be vigilant about risks that can creep into the system. At the OCC, identifying, assessing, and communicating risks to the banking system is a significant part of our job. Twice a year we publish a *Semiannual Risk Perspective* that provides a systemic view of risks facing banks and helps set priorities for our bank examiners for the next six to 12 months. Our most recent publication highlighted four risks.[6]

The first involves credit risk. While asset quality remains strong and overall underwriting is acceptable, we see the credit environment influenced by aggressive competition, tighter spreads, and slowing loan growth. These factors are driving incremental easing in underwriting

[3] S&P 2018 U.S. Bank Market Report, March 14, 2018.
[4] "National Income and Product Accounts: Gross Domestic Product: Second Quarter 2018 (Advance Estimate), and Comprehensive Update." The Bureau of Economic Analysis. U.S. Department of Commerce. July 27, 2018 (https://www.bea.gov/newsreleases/national/gdp/gdpnewsrelease.htm).
[5] "The Employment Situation—July 2018." USDL-18-1240. The Bureau of Labor Statistic. U.S. Department of Labor. August 3, 2018 (https://www.bls.gov/news.release/pdf/empsit.pdf).
[6] See Semiannual Risk Perspective, Spring 2018 (https://www.occ.gov/publications/publications-by-type/other-publications-reports/semiannual-risk-perspective/semiannual-risk-perspective-spring-2018.pdf).

practices and increasing concentrations in select loan portfolios that present heightened risk should the economy weaken or markets tighten quickly. In my experience as a banker, significant credit deterioration is the one event from which banks have the most difficulty recovering, which is why it is so important to monitor this risk closely.

The second risk stems from rising interest rates. We are moving from a long period of historically low interest rates in the United States. As we do, we need to be mindful about the effect of rising interest rates on the cost of deposits because of competitive pressures. We also need to understand the impact of rising rates on the value of long-duration and low, fixed-rate assets. Banks should be modeling these potential risks as part of sound balance sheet management. Credit risk may also increase as interest rates rise. Rising interest rates will often increase debt service costs and may affect credit affordability as well as repayment capacity of some financially stretched customers. Additionally, the yield curve has received a great deal of market attention in recent months. The spread between long-term and short-term rates narrowed to only 25 basis points this summer compared with 260 basis points in 2014, raising concerns that the yield curve could soon suggest a coming recession, because it has been an accurate indicator of recession in the past.

The third risk is one the OCC has focused on for several years now—operational risk. Operational risk remains elevated as banks adapt business models, transform technology and operating processes, and respond to increasing cybersecurity threats. Cybersecurity is top of mind for regulators and bank executives. Speed and sophistication of cybersecurity threats are increasing. Banks are continually faced with threats seeking to exploit bank personnel, processes, and technology. The number, nature, and complexity of third-party relationships continue to expand. Operational risks also grow from consolidation among larger service providers, which increases third-party concentration risk. Outages or other issues at these larger service providers that support many small and midsize U.S. banks can potentially affect wide segments of the financial industry.

The fourth risk facing U.S. banks today is compliance risk that involves the potential consequences of failing to comply with laws and regulations. Banks continue to deal with compliance risk as they manage money-laundering risk in an increasingly complex environment. At the same time, banks are tested by the high volume of changing policies and procedures necessary to comply with amended consumer protection requirements and regulatory reforms.

While credit, interest rate, operational, and compliance risks top the list of issues to manage, we are also watching risk associated with agricultural debt and banks' transition to the new current expected credit loss model of accounting. The United States is one of the major agricultural producers in the world. Potential for renewed declines in prices for grain crops, livestock, and dairy may compound three years of declining prices and increasing debt for agriculture borrowers and their ability to service debt. Meanwhile, banks that file with the U.S. Securities Exchange Commission are expected to implement the current expected credit loss standard in 2020, which may pose operational and strategic risks to some banks when measuring and assessing the collectability of financial assets. All of these risks require close scrutiny to ensure banks can continue to fuel economic growth and continue to operate in a safe and sound manner.

Initiatives to Promote Economic Opportunity

I want to shift gears now to focus on activity in the United States that is helping reduce the burden faced by banks so that they can service their customers more effectively and efficiently.

Following the financial events that began in 2008, the United States, like many countries, passed sweeping reforms to reduce risk to the financial system. While those reforms helped stop the riskiest of behaviors and recapitalize the banking system, they also had an unintended outsized effect on small and midsize banks. In May, the President signed the Economic Growth, Regulatory Relief, and Consumer Protection Act (the Economic Growth Act) with bipartisan support.[7] The OCC supported passage of the law, and I was there for the President's signing of the bill into law. I was moved by the support for the common sense reforms included in the law. This law restores an important balance to the business of banking by providing meaningful reduction of regulatory burden for community and regional institutions, while safeguarding the financial system and protecting consumers. It includes several features that will benefit community banks in particular and are consistent with my priorities as Comptroller, including reducing the number of banks subject to the Volcker Rule and providing a much simpler capital regime for highly capitalized smaller banks.

The Economic Growth Act is having a positive impact on federal savings associations by providing additional flexibility and on banks that are not designated as systemically important by appropriately raising the threshold for enhanced prudential standards and right-sizing stress-testing requirements. These, and many other reforms included in the law, help the U.S. banking system continue to create jobs and economic opportunity. Consumers, businesses, and communities alike will enjoy the benefits of these thoughtful and tailored reforms for many years.

[7] See "President Donald J. Trump Signs S. 2155 into Law." The White House. May 24, 2018 (https://www.whitehouse.gov/briefings-statements/president-donald-j-trump-signs-s-2155-law).

In addition to these broad statutory changes, I want to mention three areas where the OCC is working to promote growth and service to bank customers—innovation; short-term small-dollar lending; and our supervision of international banks operating in the United States.

Innovation has been part of the national banking system in the United States since President Lincoln created the system in 1863. The checking account, credit cards, the automated teller network, and, more recently, mobile banking have all revolutionized access to financial services in their day. Banks will continue to be innovators.

At the same time, a tremendous amount of creativity and energy is occurring in financial technology companies outside of traditional banking. In recent years, thousands of these companies have been created to deliver financial services in new ways, expand credit by leveraging new data, and give consumers more control over their financial lives. These companies hold great promise, but operating in the United States presents a few obstacles. One challenge is that to operate nationally, these new companies have had to seek licenses and be subject to the oversight of each state in which they operate. That approach is costly and prevents consumers from benefiting from innovation more quickly. That's why at the end of July, I announced the decision to begin accepting applications for national bank charters from nondepository financial technology (fintech) companies engaged in the business of banking.[8] A national bank charter allows the newly formed bank to operate across all 50 states under a single framework of rules and regulations and single primary prudential regulator—the OCC.

The decision to consider applications from innovative companies helps provide more choices to consumers and businesses and creates greater opportunity for companies that want to provide banking services in America. Companies that provide banking services in innovative

[8] See "OCC Begins Accepting National Bank Charter Applications From Financial Technology Companies." NR 2018-74. OCC. July 31, 2018 (https://www.occ.gov/news-issuances/news-releases/2018/nr-occ-2018-74.html).

ways deserve the opportunity to pursue that business on a national scale as a federally chartered, regulated bank. It is important to note, however, that a national bank charter is only one option among many for companies engaged in the business of banking. Other options include pursuing state banking charters, appropriate business licenses, and partnerships with other federal or state financial institutions. The option to apply for a national bank charter allows these companies to choose the best business model and regulatory structure for their business and strategic goals. Providing a path for fintech companies to become national banks can make the federal banking system stronger by promoting economic growth and opportunity, modernization and innovation, and competition.

Another area where we have worked is encouraging banks to offer more responsible and affordable options to meet consumers’ short-term small-dollar needs, typically between 300 and 5,000 dollars. Almost a decade ago, bank regulators in the United States took steps to protect consumers from abuses occurring in payday and predatory lending. Their actions resulted in banks stopping these services altogether, rather than reengineering them in safer, and still profitable, ways. The drop in supply led naturally to consumers turning to nontraditional sources of credit. Prices went up, and the features of these products became much less consumer friendly.

Every year, millions of consumers in the United States borrow nearly $90 billion in short-term small-dollar loans. These loans help consumers meet basic, often unplanned, needs. A repairman’s truck breaks down. An air conditioner fails in the heat of summer. Many families are ill-prepared to deal with an unexpected expense of just 400 dollars. Short-term small-dollar loans can be lifesavers for consumers in these positions. When banks are part of the solutions, bank-provided services can help lead consumers to more mainstream financial services without trapping them in cycles of debt. Banks are also better positioned than many competitors to offer products with reasonable pricing and repayment terms, and consumers also benefit from other services that banks regularly provide, such as financial education and credit reporting.

That's why in May, we published guidance encouraging national banks and federal savings associations to offer responsible short-term small-dollar installment loans. I am happy to report that we are seeing banks return to this space with careful, well thought-out products to serve their customers' needs. Repairing that truck on Friday means that repairman can still make it to his job on Monday.

The last area I want to cover this morning relates to the OCC's licensing and supervision of federal branches and agencies of foreign banks operating in the United States. Japanese banks have had a long and important history of providing credit and liquidity in the U.S. financial system. At present, there are nine Japanese institutions with U.S. operations with an aggregate $575 billion in assets as of the first quarter of 2018.[9] Foreign banks doing business in the United States or seeking to do business also have a choice to operate on the state or national level. If a foreign bank decides to operate on the state level, the bank is required to obtain a license in each state it operates in for each entity it licenses. In a large banking company that can mean licensing in five to 10 states, resulting in five to 10 different entities and regulators. That adds complexity and operating costs and, in my view as a banker, may not be the most efficient approach to conducting banking in the United States. While it may make sense for some foreign banks, other banks could benefit from operating under a single regulatory framework with one prudential regulator—the OCC.

The OCC strongly supports the dual banking system in the United States. The decision to operate under a state or federal license is a business decision available to banks. It is a choice

[9] FFIEC 002 reports: US Branches and Agencies of Foreign Banks.

that banks should be able to make based on their business model and goals. In considering that choice, banks should be aware that the OCC is well positioned and qualified to provide effective and efficient supervision of federal branches of foreign banks operating in the United States because of its experience supervising the largest, most internationally active banks in the country. The OCC has a long history of supervising federal branches of foreign banks operating in the country. In many cases, there are supervisory efficiencies gained by consolidating the supervision of branches of foreign banks with the supervision of the national bank subsidiary of the parent company, which the OCC already supervises. The result is more complete, more efficient, and, importantly, more thorough regulation of the institution.

The OCC has licensing, legal, and supervision experts who can provide insight into making a sound business decision about whether to operate nationally or state by state. We understand the importance of this decision, the nuances, and the challenges banks face. Operating under federal supervision is not right for every bank, but it can make sense depending on your business model.

Conclusion

I want to end by saying again how much I appreciate the invitation to come here and share my views. I have great optimism for banking in the United States and globally and appreciate everyone in the room who has chosen to work in the field of banking, whether as a banker or regulator. Bankers and regulators really share the common goal of a system that serves customers well and ensuring that system promotes economic opportunity for the individuals, businesses, and communities it serves. Thank you for your attention and good work.