Remarks

By

Thomas J. Curry
Comptroller of the Currency

on

The OCC's *Semiannual Risk Perspective,* Spring 2016

July 11, 2016

Thank you for joining us on this call to discuss the OCC's *Semiannual Risk Perspective*. We began publishing our assessment of the risks facing the federal banking system in 2012 to bring greater transparency to our views and priorities and to promote greater risk management across national banks and federal savings associations. Since that time, the report has become regular reading for industry participants, analysts, and, of course, bank supervisors.

This report reflects data as of the end of 2015, and shows the performance of federally chartered banks improved from 2014. The banking sector benefited from the improving economy with broad-based loan growth, driven by commercial and industrial and real estate lending. Income and profitability were up, particularly at banks with less than $1 billion in assets, which had return on equity that exceeded 10 percent on average. Large banks net income also improved, but higher provisioning expenses partially offset gains in net interest income and lower overhead. The improvement in banks' performance is also reflected in the decreasing number of 4- and 5-rated national banks and federal savings associations, which fell 34 percent in 2015. All of these indicators suggest a strong and healthy federal banking system. However, despite these improving indicators, as regulators, we must remain on guard and our top concerns for the banking system remain strategic, credit, operational, and compliance risks.

The banking environment continues to evolve, with growing competition among banks, nonbanks, and financial technology firms. Some banks are struggling to find viable business models, while others are increasingly adopting innovative products, services, and processes in response to evolving customer demands and the entrance of new competitors. Doing so often involves assuming unfamiliar risks, including expanded reliance on third-party relationships. Banks may face heightened strategic planning and governance risk if they do not use sound risk management practices that align with their overall business strategies.

It's at this stage of the cycle that we also see strong loan growth combined with easing underwriting to result in increased credit risk. While leveraged lending and auto lending remain concerns, CRE lending and concentration risk management has become an area of emphasis for regulators. CRE portfolios have seen rapid growth, particularly among small banks. At the end of 2015, 406 banks had CRE portfolios that had grown more than 50 percent in the prior three years. Of note, more than 180 of these banks more than doubled their CRE portfolios during the past three years. At the same time we are seeing this high growth, our exams found looser underwriting standards with less-restrictive covenants, extended maturities, longer interest-only periods, limited guarantor requirements, and deficient-stress testing practices.

While not at the same level of risk, we are also monitoring effects of continued low oil prices and the increase in marketplace lending. As a result of the decline in oil prices since the summer of 2014, U.S. oil companies have idled 70 percent of their rigs, reduced capital spending, and cut more than 100,000 jobs, with the greatest impact on Louisiana, North Dakota, Oklahoma, West Virginia, and Wyoming. And, direct bank lenders to the oil and gas industry have seen a substantial rise in problem loans that we are monitoring closely.

In contrast to oil and gas related-lending, marketplace lending grew rapidly in 2015. Marketplace lenders originated nearly $29 billion in loans in 2015, although they still represent a small portion of the $3.6 trillion consumer-lending sector. We also see an increasing number of relationships between banks and marketplace lenders. While the OCC strongly encourages responsible innovation that provides fair access to financial services and fair treatment of consumers, we have also stressed that banks should have effective risk management to ensure such innovation aligns to their long-term business strategies.

We are also keeping our eyes on operational and compliance risks—both of which remain elevated. Operationally, banks are dealing with existing and constantly evolving cybersecurity threats and increasingly rely on third parties for essential services. These areas require heightened management attention and continuous vigilance. On the compliance front, BSA/AML risk continues to increase. Technological developments in enhanced delivery platforms for bank products may create new vulnerabilities to cyber threats and criminal activity, while traditional concerns—such as trade-based money laundering and bulk cash smuggling, including via armored car service and funnel account activity—remain risks to banks. In addition to BSA/AML risks, we have identified compliance with the Military Lending Act and the Truth in Lending Act as key risks for the federal banking system. Banks have more work to do to ensure full compliance with these laws. The OCC's fiscal year 2017 examination strategies will incorporate an assessment of compliance with the rules that implement these laws, as well as an assessment of banks' overall compliance management systems and compliance efforts.

Before I close, I want to thank the staff members who put in so much work to deliver this report twice a year. It takes a great deal of effort and makes a significant contribution to the industry by providing focus and clarity for risks facing national banks and federal thrifts. Now let me turn things over to Deputy Comptroller for Supervision Risk Management Darrin Benhart who can add color to some of these issues.