Supervisory Spotlight

A Regulator's Perspective on Issues Facing Western Banks

Financial Institution Supervision and Credit
FEDERAL RESERVE BANK
OF SAN FRANCISCO

July 2015

Greetings!

Welcome to the first Supervisory Spotlight under the banner of our newly named division: Financial Institution Supervision and Credit, or FISC. Yes, after many, many years as Banking Supervision & Regulation, our division has a new name. Ultimately, two factors weighed heavily in both the decision to change our name and in the ultimate name.

First, the Reserve Bank's Chief Financial Officer, Donald Lieb, retired on June 1. Before his retirement, Don headed the Credit Risk Management (CRM) function, which included oversight of the Reserve Bank's discount window. As part of our ongoing desire to identify operational synergies, we ultimately decided to merge the CRM function and BS&R into a combined division. There was a really good business case for this merger, given that both groups are central bank functions, focus on financial institutions, and share common stakeholders, knowledge, and expertise. Second, the nature of banking supervision has evolved greatly over the years. We truly have evolved from being "bank supervisors," and BS&R no longer captured the full scope of our responsibilities. So we are now FISC, supervising a broad array of financial institutions and extending credit to depository institutions through the discount window.

Keeping with the theme of change, you're no doubt aware of the numerous changes that have occurred in banking and bank supervision since the financial crisis. A significant goal of the post-crisis efforts to strengthen our banking system was to better ensure that the largest banks have mechanisms and resources to withstand most forms of economic and financial stress while distinguishing between large bank and community bank supervision. Our May 22, 2015, San Francisco Fed blog, Building a More Resilient U.S. Banking System, highlights a recent article, How Is Banking Safer Following the Financial Crisis?. These two resources discuss ten ways that the Federal Reserve, often working with other regulators, has helped to ensure the safety and soundness of our financial system. More recently, the second quarter 2015 issue of *Community Banking Connections* included an article, Some Thoughts on Community Banking: A Conversation with Chair Janet Yellen. In a Q&A format, Chair Yellen discusses the advantages of and challenges facing community banks, the Federal Reserve's efforts to solicit the views and address the concerns of community bankers, and Federal Reserve resources available to community banks.

Another area where we will likely see some change relates to bank's net interest margins, or NIM. A second quarter 2015 *Community Banking Connections* article by the Kansas City Fed discusses What Explains Low Net Interest Income at Community Banks?. The results of the authors' study suggest that low NIM is not the new normal for community banks and that, while NIM may be unlikely to return to the high levels of the early 1990s, it is likely to rebound significantly as the economy improves. As we reported in the first quarter 2015 First Glance 12L , loans at Twelfth District commercial banks grew over 12 percent in the year ended March 31, 2015. This sign of economic improvement also may portend future improvement in the NIM.

A third area where all banks may experience change is in how their customers are touched by virtual currencies. A recent *Community Banking Connections* article, What Community Bankers Should Know About Virtual Currencies, reviews the virtual currency landscape and raises some thoughtful points about the impact of customers trading in or accepting virtual currencies. This is definitely an evolving area, and the article provides some good food for thought.

Finally, I'd be remiss if I didn't mention another area of change for many community banks: the Consumer Financial Protection Bureau's changes affecting home mortgage lending. Over the years, the Federal Reserve System's *Consumer Compliance Outlook* publication has discussed many of these changes in significant detail. The first quarter 2015 article, The Expanded Scope of High-Cost Mortgages Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, raises some good reminders about new rules for high-cost mortgages.

In closing, I remind you that it is not too late for your voice to be heard as the agencies consider future regulatory changes. As I mentioned in the April issue of Supervisory Spotlight, the agencies are conducting a decennial regulatory review required by the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA). You can get more information on the related series of public meetings and notices for comment on the FFIEC's EGRPRA website. I encourage you and your teams to take advantage of these opportunities to provide constructive input into the discussion on regulatory burden, whether in person or in writing.

As always, I appreciate feedback and suggestions for topics that are of particular concern to your institutions.

Teresa Curran

Teresa.Curran@sf.frb.org

Resources

You can view additional *Community Banking Connections* articles and subscribe to an electronic or hard copy of the publication at http://www.communitybankingconnections.org/. You can also view additional *Consumer Compliance Outlook* articles and subscribe to that publication at https://www.consumercomplianceoutlook.org/. Please also consider subscribing to receive notifications of our Reserve Bank's Banking Supervision publications and programs at http://www.frbsf.org/our-district/subscriptions/financial-institution-supervision-credit-subscriptions/.