Remarks by

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Good morning. I want to thank The Clearing House for having me here. I appreciate venerable institutions, and this is one of the rare organizations that's older than the one I'm privileged to lead—even if it is just 10 years older. With The Clearing House and the Office of the Comptroller of the Currency (OCC) dating to the mid-19th century, both institutions have weathered Great Depressions and Great Recessions and have lived to tell the tales and share the scars of the experiences. With such great history and institutional memories, I am often disappointed how quickly some forget the lessons of more recent events, particularly what brought the financial system to the cliff in 2008 and what has put our banks and our economy on much firmer ground since. Today, in my third speech before The Clearing House as Comptroller, I want to take this opportunity to remind *us* of the important lessons of the last crisis—particularly for our large complex banks—the value of strong capital, the need for ample liquidity, and the importance of effective supervision.

With regard to capital, our banking system is now as well capitalized as any in my professional memory. We've had six years of steady progress. This year's Federal Reserve's stress tests show common equity at levels more than double that of the first quarter of 2009.[1] In

[1] See *Comprehensive Capital Analysis and Review 2016: Assessment Framework and Results*. The Board of Governors of the Federal Reserve System. June 29, 2016 (http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20160629a1.pdf).

raw numbers, that's a $700 billion increase in common equity capital. At this level even under the *most severe* scenario considered, the 33 largest bank holding companies would continue to be well capitalized[2] and capable of lending into a recession. Strong capital like this will reduce the severity and length of the next downturn—*if* capital remains strong.

Not even a decade from the last crisis, some thoughtful people are beginning to question whether capital requirements have gone too far. A few critics suggest today's capital requirements unduly restrict lending and limit economic growth. It's a legitimate policy question, but the last crisis answers with a vivid example of what happens when banks fail to hold capital levels commensurate with their risks. The benefits of a robust banking system built on strong capital should not be forgotten in any debates about regulatory reform and striking the right balance in capital standards going forward. Our capital requirements help make our largest banks more resilient and allow them to be a source of strength for the nation and global economy.

Another lesson from the crisis that we need to remember is the danger of excessive leverage. We have long recognized that strong risk-based capital alone cannot ensure the safety and soundness of large complex banks. Once markets begin to question the quality and quantity of capital levels, it may already be too late. For this reason, we have employed leverage ratios to serve as an additional line of defense, or backstop, to the risk-based capital measures. We have taken a proportionate approach to constraining bank leverage by employing a slightly more sophisticated leverage ratio measure for the largest banks.[3]

One of the key features of these leverage ratio metrics for larger banks is that they capture elements that contribute to leverage that are not captured by simpler measures that focus

[2] Average calculated from on table 4, page 16 of *Comprehensive Capital Analysis and Review 2016: Assessment Framework and Results.*

[3] NR 2014-118, "Agencies Adopt Supplementary Leverage Ratio Final Rule." September 3, 2014 (http://www.occ.gov/news-issuances/news-releases/2014/nr-ia-2014-118.html).

exclusively on a bank's balance sheet. And as we have done with capital standards more generally, we have required our largest banks to meet more stringent leverage ratio requirements than smaller institutions given their systemic importance.

But here too, some want to water down the ratios by manipulating what is included or excluded from consideration. Weakening the ratio through special exclusions only undermines our original intent and weakens the protection against excessive leverage. The essence of assessing a bank's leverage is about comparing its equity to its assets, and carving out various assets would cut against the very meaning of leverage. In addition, if a relatively simple and straightforward metric is riddled with exceptions, it will become much more complicated and difficult to understand, which will make market participants less trusting at the most critical points of a downturn, and when investors most need a clear understanding of a bank's leverage and capital.

The next lesson that I want to stress is the need for ample liquidity. The lack of liquidity contributed as much to solvency issues in 2008 as weak capital did.

Since then we have taken prudent steps to ensure ample liquidity by implementing the Liquidity Coverage Ratio (LCR) and proposing the Net Stable Funding Ratio (NSFR). These two ratios complement each other to push covered banks to hold ready resources to meet short-term cash outflows and to shift to more stable, longer-term funding. Liquidity can disappear quickly without taking steps to ensure its availability, and the loss of liquidity can be devastating to a company and have contagious effects on the system as a whole.

Strong capital, limits on leverage, and ample liquidity bolster the strength of our banking system. We can see that on your balance sheets today. Tier 1 common equity is nearly 13 percent of risk-weighted assets, up from 9 percent in the fall of 2008. The leverage ratio is now at

9.3 percent, almost one-third higher than in 2008. And, liquid assets have achieved a 30-year high of 16 percent of total assets.

Those who suggest you can't be competitive and profitable with such high standards may be proved wrong. The strength of U.S. banks have improved their competitiveness not weakened it. Last year, revenue for the top five U.S. banks was more than double that of their European counterparts, and U.S. banks' pre-tax profits of $33.5 billion dwarfed the European banks' $4.2 billion. U.S. banks are better today because of the rigor of the new standards, and how quickly we implemented them. They are strong and profitable *because* of earlier recognition of losses and troubled assets and the discipline to work through those issues aggressively.

But, financial numbers don't tell the whole story. That's why holistic supervision is so important, and that's why the CAMELS rating system considers factors such as the quality of management and compliance. It's impossible really to be safe and sound if you don't comply with the laws and regulations intended to protect the system and the consumers, businesses, and communities it is intended to serve. Recent revelations about sales practices bears this out. The overall health of a bank results from the quality of its management, how it tackles operational risk, and its commitment to compliance and treating customers fairly and incenting employees to do the right thing each day. It's true that a steadily improving economy and better financial fundamentals has helped banks' overall ratings, but the improvement we see on the ground in the banks reflects hard work by bankers and examiners. We were right to spend as much time on operational risk and compliance issues over the last several years as other more traditional safety and soundness measures, because we have seen the major issues since the crisis reflect failures in these areas. Since 2010, the number of troubled institutions (rated 4 or 5) has fallen from a high of 196 at the end of 2010 to fewer than 50 at the end of 2015. That is solid progress that reflects the value of strong supervision and improved bank governance, but it is progress that requires vigilance to maintain.

After more than three decades overseeing financial institutions of all shapes and sizes, I know supervision is the regulators' best tool to affect behavior and promote strong risk management at the institutions we oversee; and while it is appropriate to reassess banking laws and regulations periodically, we must never settle for "light-touch" supervision. If we do, the OCC and the industry will suffer. It is not the job of bank regulators and examiners to effectively nullify laws that Congress enacts through selective enforcement. Less stringent oversight ultimately imperils the business models of large, systemically important institutions because these banks will face greater risk of breakup if the public believes they are supervised less rigorously or are immune to remedial actions that would otherwise apply to smaller institutions. Guarding against this risk is simple. We need to maintain high professional standards for the OCC and high expectations of our largest banks if we are to have a credible system.

To improve risk management across the industry, particularly among the largest banks we supervise, we set enforceable heightened standards for management and boards of directors that established clear expectations for governance and risk management. These standards grew from "boots-on-the-ground" observations made by examiners during the crisis, which were distilled into enforceable standards for our largest banks. We supervise against those standards today and are seeing significant improvement.

While we have clearly come a long way from my first speech here in 2012, my job is to ask how well we—regulators and bankers—are preparing for the next stress event or downturn. And, now is not the time to change course or weaken the protections and safeguards we have put in place since the last crisis. We cannot return to the same practices and weaker safeguards that resulted in the crisis we experienced in 2008.

We must remain vigilant about the levels of capital and liquidity in good times so they will be there to serve as a bulwark during the next recession.

We have to limit concentrations in assets such as commercial real estate that have historically been problems when the tide turns, and we need to guard against the effects of underwriting that has loosened each of the last four years. These are old threats we know well, but we also have to continually up our game against new threats, such as evolving cyber attacks, so that our nation's banks and the system as a whole can effectively withstand these events and recover when they occur.

We must also continue to raise the standards of governance at our banks so that leadership remains sound and boards provide a credible challenge to management. The OCC's heightened standards require that a percentage of national banks board members be independent. This is one area that may require further work. For instance, some national banks have split the roles of Board Chairman and Chief Executive Officer to clearly delineate roles and governance of the institution and eliminate potential conflicts of interest that exist when the same individual serves in both roles. We should consider whether this structural change by some national banks makes sense for all federally supervised banks, or at least the largest most complex ones. In the interest of transparency, information on national bank boards and officers should be made available to the public by the OCC or the institution. Such actions make responsibility and authority more clear and promote confidence that such important institutions are well managed and governed.

I am glad that our banks and the banking system *are* stronger today, but now is not the time to let our guard down. Those who have been in this business for more than one cycle know a downturn will come. Effective regulation and supervision will help ensure that the trough will not be so deep or so wide. Those who forget or choose to ignore the lessons of the last crisis do so at their own peril and increase the risk to all of us.

The vast majority of my comments today have focused on the condition, performance, governance, and supervision of our largest and most complex financial institutions. There is no denying that these institutions with $500 billion, a trillion, or even $2 trillion in assets can have a tremendous impact on our banking system and the nation's economy if something goes wrong. They deserve added attention, higher standards, and more robust levels of capital and liquidity than smaller institutions. That's why in implementing these rules since the crisis, we have been careful to moderate the impact of these standards on smaller banks that serve local communities across the country.

America's community banks are stronger today. Return on equity among community banks has nearly recovered to pre-crisis levels, and loan growth has been steady.
Where it has made sense, we have worked to remove unnecessary burden by simplifying the call report, lengthening the exam cycle for well-managed banks, and encouraging collaboration. But small banks too should be careful not to undo the progress they've made since the crisis. To remain strong and healthy, community banks, and their examiners, need to focus on strategic risk, rising credit risk from stretching for yield while relaxing underwriting standards, expansion of new technologies, and compliance issues.[4]

As I close these remarks so that we have time for questions, I want to stress that regulators and the industry *can* take some pride in how far we've come since the crisis. Those of

[4] See Fiscal Year 2017 Bank Supervision Operating Plan. September 14, 2016 (https://occ.gov/news-issuances/news-releases/2016/nr-occ-2016-112a.pdf).

us who were there in October 2008 know just how dark the storm clouds were, and how much brighter the skies are today.

But acknowledging our progress cannot lead to complacency lest we repeat our own history, which I for one hope to avoid.

Thank you again for having me here today and as time permits, I'm happy to try to answer some questions.