

## The Mission and Strategy of OCC Economics

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The Mission of the Office of the Comptroller of the Currency (OCC) is to ensure that national banks and federal savings associations operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations. The mission of OCC Economics, like every other part of the OCC, is to do all that it can to support the OCC's mission. Economics houses a unique set of capabilities—knowledge of conceptual frameworks and facts, and problem-solving capabilities that come from that knowledge. The logic of economics and the evidence that supports that logic provide the necessary basis for thought leadership—internally and externally—that no other kind of thinking or evidence can provide.

The unique skills possessed internally by OCC economists are central to designing and implementing an effective framework for prudential and consumer protection regulations and the supervisory system that enforces them. As the OCC faces ongoing conceptual challenges—such as designing the appropriate regulatory and supervisory system for the chartering of novel banks<sup>1</sup>—it must rely on economists to provide essential feedback to supervisors and examiners about existing practices and suggest improvements to the regulatory and supervisory frameworks based on economic analysis.

At slightly over 100 in number, the economists at the OCC are engaged in a broad range of activities, including participating in the examinations of national banks, providing advice to OCC leadership and staff on a variety of issues, engaging in research on bank performance and bank regulation, and externally communicating research findings to the public.

OCC Economics is in the process of building several working groups. These working groups include not only economists, but also others in the OCC who have subject matter knowledge and an administrative responsibility related to the set of questions that will be addressed by a particular working group. Topic-based working groups foster integration within Economics and across OCC departments, help economists apply their experience and knowledge from supporting bank examinations to better identifying and addressing the big questions of central importance to the OCC and the federal banking system, and help non-economists contribute to the economics research agenda. These collaborations also improve everyone at the OCC's understanding of future data needs within the OCC.

OCC Economics is undertaking a major expansion of how it communicates with the public. Two new working paper series devoted to banking research will foster productive internal dialogue to improve ongoing research. The Economics web page will contain various weekly, monthly, and quarterly features that examine issues of current interest related to bank performance, bank regulation and supervision, financial markets, and the economy. OCC economists also have

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<sup>1</sup> The term novel bank refers to a bank (usually a fintech firm) with a novel business model. Novel banks can apply for any of the types of bank charters granted by the OCC.

introduced a new feature that explores important moments in banking and financial history, which is especially useful when reflecting on important changes underway today.

## **Working Group Topics**

Working group topic areas examine questions that are: (1) of central importance to the OCC's mission as a bank chartering authority, regulator, and supervisor; (2) related to important regulatory or supervisory initiatives that are already underway at the OCC; (3) novel enough and specific enough that there are important opportunities for a research focus on this topic to produce timely thought leadership by the OCC; and (4) connected to the OCC's technical comparative advantages and unique data resources.

**Nonperforming Loans (NPL).** This working group will provide immediate knowledge about how the COVID-19 pandemic is affecting the banking system, build a new in-house capability for forecasting NPLs, create opportunities for publishing in professional journals, and develop knowledge enabling the OCC to assist member banks with CECL compliance.

**CRA Regulation.** The OCC recently has undertaken reforms in the measurement of compliance with the Community Reinvestment Act (CRA). There is already a collaborative group across the OCC involved in discussing and assessing the new CRA regulatory scoring framework and considering how best to implement it. The new CRA rule will also create new data, which OCC economists expect will help them better model the supply of credit to various communities. This data may also allow the economists to further improve the existing rule to make it more effective, transparent, and consistent in its treatment of banks and their communities.

**Bundling, Unbundling, Value Creation in Banking; Fintech Chartering and Its Regulation.** This is a working group divided into two sub-groups—one on bundling, unbundling, and bank valuation analysis; and another on the fintech future of banking services and the chartering of novel banks. Initially, it makes sense to combine these sub-groups into one large group because there are conceptual synergies between the two sets of questions they address (which require knowledge of issues revolving around corporate structure, valuation, and industrial organization, as well as the economics of network structure and stability). The current OCC initiatives in chartering novel banks and considering the advantages of allowing banks to unbundle financial services are closely aligned with this working group's focus.

**Fintech and Financial Inclusion.** This working group examines the potential role of new technologies in promoting greater financial inclusion. This working group will also be closely linked to the ongoing support for the OCC's Project REACh (Roundtable for Economic Access and Change) initiative.

**Stress Tests 2.0.** Stress tests are a recent invention (the stress tests that the OCC implements were mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010). This is an aspect of prudential regulation that is likely to see major improvement over the next decade. Stress testing currently focuses on the effects of shocks on tangible assets, and assesses the performance of the stressed bank on the basis of its exit ratio of tangible net worth to tangible assets. But banks are service companies, and intangible assets (which measure the discounted

value of current and anticipated cash flows that are unrelated to tangible assets on the balance sheet) are a major driver of banks' enterprise values. *Stress is properly defined as a sudden change in the value of the whole banking enterprise, and a successful exit from a stress test is properly defined as its ability to exit with a sufficiently high ratio of enterprise equity value relative to total assets.* The frontier of stress testing is to find ways to provide measures of bank enterprise value and stress that reflect this understanding.

**Restarting a Private Mortgage Market.** Private label mortgage-backed securities (MBS) have shrunk dramatically since 2008. What can be done (consistent with safe and sound banking practice) to restore the private sector's role in the secondary mortgage market? The answer is not obvious. It could be that the exemption from the Qualified Mortgage (QM) and Qualified Residential Mortgage (QRM) rules given to Fannie Mae and Freddie Mac, combined with the Federal Housing Finance Authority's willingness to permit high-risk mortgages (i.e., those that violate the QM/QRM standard) provide an unbreachable competitive advantage to Fannie Mae and Freddie Mac. On the other hand, it may be that legal reforms or innovative technologies could change the private MBS landscape. This working group would take a close look at competition in the MBS market and consider regulatory or policy changes that might be able to restore a greater private role.

**How Will Commercial Real Estate Recover from Covid?** The COVID-19 pandemic not only caused short-term disruption to the economy and the commercial real estate market, it also accelerated behavioral changes in the way people work and live, with potentially wide-ranging impacts on the values of different types of commercial property. This working group tracks those changes closely, by location and property type, connecting real estate property changes to local changes in economic fundamentals, and investigating the implications of those changes for banks.

## **Conclusion**

This is an exciting time for the Economics Department at the OCC, resulting from the innovative environment for banking today and the continuing challenges of regulation and supervision, which create new opportunities for the Economics Department to work in concert with other OCC staff and demonstrate the importance of economic analysis to realizing our collective aspirations for continually improving the bank regulatory and supervisory process.