

Global Credit Research - 17 Jun 2010

Des Moines, Iowa, United States

## Ratings

Category	Moody's Rating
Outlook	Stable
Bank Deposits	Aaa/P-1
<b>Parent: Federal Home Loan Banks</b>	
Outlook	Stable
Senior Unsecured	Aaa
Other Short Term	P-1

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## Key Indicators

### Federal Home Loan Bank of Des Moines

	[1]2010	2009	2008	2007	2006
ROAA (%)	0.19	0.21	0.18	0.21	0.20
ROAE (%)	4.25	4.46	3.88	4.25	3.91
Net Interest Margin (%)	0.32	0.28	0.35	0.36	0.35
Advances (\$bil)	33.03	35.70	41.90	40.41	21.86
Investments (\$bil)	23.24	20.79	15.37	9.24	8.22
Assets (\$bil)	64.62	64.66	68.13	60.77	42.04
Equity (\$bil)	2.85	2.91	3.02	3.05	2.25
Liquid Assets/ST Debt (%)	60.35	48.11	26.26	19.30	23.68

[1] For the quarter ended March 31, 2010

## Opinion

### SUMMARY RATING RATIONALE

Federal Home Loan Bank of Des Moines' (FHLBank) Aaa/Prime-1 long- and short-term deposit ratings reflect the combination of the following factors: 1) a stand-alone Baseline Credit Assessment (BCA) of 5 (on a scale of 1 to 21, where 1 represents the lowest credit risk), 2) very high cooperative support from the FHLBank System, 3) very high support from the U.S. government (Aaa debt rating).

The FHLBank of Des Moines' BCA of 5, which is an A1 equivalent on Moody's long-term debt rating scale, reflects Moody's opinion about the FHLBank's intrinsic or stand-alone financial strength and exclude extraordinary support, either from the FHLBank System or the U.S. Government. The rating incorporates the FHLBank's modest risk-adjusted profitability, sound liquidity and excellent asset quality on both its advance and mortgage loan portfolios. The FHLBank's exposure to private-label residential mortgage back securities is not sizable at \$35 million.

The FHLBank of Des Moines' BCA of 5 does not benefit from support from the FHLBank System given the FHLBank System's BCA of a 5 (A1 equivalent). On the other hand, Moody's very high U.S. government support assumption lifts the FHLBank of Des Moines' deposit ratings to Aaa.

### Credit Strengths

Joint and several liability reduces default risk of Systemwide liabilities

Central role as liquidity provider for banks and other financial institutions

Excellent asset quality reflects conservative underwriting standards and quality-monitoring policies

### Credit Challenges

Narrow charter and bank consolidation constrain growth and profitability

Substantial borrower concentration

### **Rating Outlook**

Moody's stable outlook for the FHLBank of Des Moines' rating reflects the FHLBank's consistent returns and its low exposure to private-label MBS. Moody's expects the FHLBank of Des Moines to conservatively manage its business in achieving a modest but stable risk adjusted return.

In addition, Moody's expectation that the FHLBank System will continue to receive strong bipartisan political support, that there will be minimal changes, if any, to its government sponsored enterprise (GSE) status over the long - term.

### **What Could Change the Rating - Up**

Factors that would lead to an upgrade of the FHLBank of Des Moines' baseline credit assessment include capital levels well in excess of regulatory requirements (e.g., capital-to-assets ratio consistently 50 bps above the regulatory requirement - currently 4.0%), consistent risk-adjusted returns while maintaining strong asset quality.

### **What Could Change the Rating - Down**

Factors that could lead to a downgrade of the Aaa/Prime-1 long- and short-term deposit ratings and baseline credit assessment include a material decline in profitability (quarterly net losses over four quarters), significant asset-liability mismatches, or material changes in asset quality.

In addition, any regulatory or statutory changes to the System's mission or GSE status that alters the FHLBank's risk profile could also impact the ratings. However, Moody's views these potential events as highly unlikely to occur.

### **DETAILED RATING CONSIDERATIONS**

The FHLBank of Des Moines lends to member institutions in the form of advances, which are generally short-term and over-collateralized, minimizing the credit risk on these loans. Moody's baseline credit assessment represents our opinion of the likelihood that the institution will require extraordinary support from an external party. The high BCA of 5 reflects FHLBank of Des Moines' strong credit culture, stable, though moderate, profitability, and the benefits associated with the joint and several liability of the FHLBank System. Below are the detailed rating factors that influence the FHLBank's ratings and outlook.

#### **Baseline Credit Assessment**

##### **Profitability**

FHLBank of Des Moines' modest but consistent profitability (as measured by ROAA) reflects primarily low risk profile of its asset base. ROAA was 0.19% for the three months ended March 31, 2010, compared to 0.21% and 0.18% for years end 2009 and 2008, respectively. The five-year standard deviation of ROAA for 2005 to 2009 was 0.13%, which was well below the 0.53% standard deviation for US banks rated Aa or higher.

Similar to many other FHLBanks, the FHLBank of Des Moines has significant borrower concentration: its top five advance borrowers represented 41% of advances outstanding as of March 31, 2010. Within the top five advance borrowers, the largest borrower accounted for 17% of the FHLBank's total advances at March 31, 2010. Large single-name exposures, besides they increase counterparty credit risks, heighten the risk that bank consolidation among these institutions could lead to profitability constraint as bank consolidation will likely reduce demand for advances.

##### **Capital Adequacy**

FHLBank of Des Moines is required by legislation to maintain minimum regulatory capital level of 4.0% of its total assets. At March 31, 2010 the capital ratio of the Des Moines Bank was 4.39%, down from 4.57% at year end 2009 and 4.66% at year end 2008. The decline from year end 2009 to March 31, 2010 was primarily due to a decrease in activity-based capital stock. Although the ratio has declined, it exceeds the regulatory requirement and we do not expect it to decline below minimum capital level. In Moody's view, capital levels reflect the low risk profile of the FHLBank's asset base which is largely comprised of advances to member banks (51% of total assets as of March 31, 2010).

##### **Interest Rate Risk Management**

The FHLBank of Des Moines conservatively manages its interest rate risk exposures through the use of debt with similar characteristics to the FHLBanks assets, as well as derivatives. The FHLBank's primary asset is advances (51% of total assets), which come in a variety of types, including fixed rate, variable rate, callable by the FHLBank as well as putable advances. With a putable advance, the FHLBank purchases a put option from the member that allows the FHLBank to terminate the fixed rate advance on specified dates and offer, subject to certain conditions, replacement funding at prevailing market rates. Prepayment fees, which mitigate interest rate risk, are also a common feature of advances.

The FHLBank of Des Moines' policy limits the market value of capital stock (MVCS) to 5% and 10% declines from the base case in an up and down 100 basis point and 200 basis point interest rate shift, respectively. During the first quarter of 2010 and all of 2009, the Bank's projected MVCS in the down 200 basis point rate shift scenario fell below the 10 percent policy threshold loss. However, The FHLBank's Board of Directors waived the 200 basis point down policy limit due to the low interest rate environment.

##### **Asset Quality and Credit Risk Management**

Moody's believes that the asset quality of the FHLBank of Des Moines is exceptional. Advances represent 51% of total assets as of March 31, 2010, while the FHLBank's investment portfolio represents 36%. The investment portfolio comprised mostly of fed funds sold and US government and agency securities with a very small private label MBS portfolio. Advances are over-collateralized and the FHLBank has never incurred a loss on an advance in its 77 year history. The FHLBank of Des Moines has advance concentration, similar to other FHLBanks. The top five advance borrowers represented 41% of advances outstanding as of March 31, 2010. High single borrower concentration increases the FHLBank's counterparty risk.

The FHLBank participates in the MPF, which represents 12% of its total assets. The credit quality of MPF loans has been exceptional. The FHLBank of Des Moines charged off only \$127,000 in mortgage loans during the first three months of 2010.

#### Liquidity and Funding

FHLBank funding spreads tightened considerably during the second half of 2009 resulting in margin expansion as its liabilities re-priced quicker than its assets in a declining rate environment. The FHLBank's GSE status has provided it with consistent and stable access to the debt market. The FHLBank's internal sources of liquidity are modest. As of March 31, 2010, the FHLBank of Des Moines had approximately \$23 billion in short-term consolidated obligations, which includes discount notes and bonds maturing within a one year period. In total, short-term debt comprised about 40% of total debts, compared to 67% at March 31, 2009. The decline was due to the fact that the FHLBank was able to fund a greater portion of its financing needs with longer maturity debts while interest rates and market demand for such debt returned to more historically normal levels. Liquid assets were approximately 60% of short-term debt as of March 31, 2010. Liquid assets include cash, cash equivalents, interest-bearing deposits, reversed repos, federal funds as well as portfolios of trading and available-for-sale investment securities. These assets are of high quality, with the investment securities portfolio comprised of U.S. Treasury and agency securities, state and local housing agency obligations and MBS.

The Federal Housing Finance Agency, the regulator of the FHLBanks, requires each FHLBank to maintain sufficient liquidity, through short-term investments, in an amount at least equal to an FHLBank's anticipated cash outflows under two different scenarios. One scenario assumes that an FHLBank cannot access the capital markets for a period of between 10 to 20 days, with initial guidance set at fifteen days and members do not renew any maturing, prepaid and called advances. The second scenario assumes that an FHLBank cannot access the capital markets for a period of between three to seven days, with initial guidance set at five days during which members will automatically renew maturing and called advances for all members except very large, highly rated members. In Moody's view the new liquidity requirements are modestly positive.

In addition, the FHLBank met all other internal liquidity requirements at March 31, 2010.

#### Other

A significant underpinning of the Baseline Credit Assessments is the joint and several nature of the consolidated obligations. The financial strength of individual FHLBanks is very sound, and the joint and several liability contributes to the overall strength of the FHLBank System by narrowing any ratings differences among the individual Banks that could exist were ratings to exclude the joint and several feature. As a result, the ratings of the weakest FHLBanks are increased, and the ratings of the strongest are lowered.

#### Support and Dependence

The FHLBank's high dependence and support levels are based on the importance of the System to its member institutions, and their ability to support housing finance and community development.



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