

The Federal Home Loan Bank System Is Profitable In First-Quarter 2010 With Manageable Nonagency Credit Deterioration

Primary Credit Analyst:

Daniel E Teclaw, New York (1) 212-438-8716; daniel_teclaw@standardandpoors.com

Secondary Credit Analysts:

Vandana Sharma, New York (1) 212-438-2250; vandana_sharma@standardandpoors.com

Sunsierre Newsome, New York (1) 212-438-2421; sunsierre_newsome@standardandpoors.com

NEW YORK (Standard & Poor's) May 4, 2010--On April 30, 2010, the Federal Home Loan Bank System preliminarily reported combined net income for first-quarter 2010 of \$325 million, down 41% from \$552 million in fourth-quarter 2009 and down 6% from \$345 million in first-quarter 2009. The System's operating performance is in line with our expectations.

The System's capital is satisfactory as expected member demand for advances has remained weak, and other-than-temporary impairment (OTTI) charges against private-label residential mortgage-backed securities (RMBS) have started to moderate. Eleven of the 12 FHLB System banks reported positive net income in first-quarter 2010, compared to 10 in fourth-quarter 2009.

FHLB-Topeka preliminarily reported a \$30 million loss in first-quarter 2010, primarily due to derivative losses. This compares with a \$46 million profit in fourth-quarter 2009 and a \$61 million profit in first-quarter 2009. Individual FHLB System bank detailed results will be available in early May with the filing of each entity's SEC Form 10-Q.

The System continues to hold satisfactory capital for its risks, and management teams are holding on to or cautiously returning capital stock to member banks where they are permitted to do so. All FHLB System banks were in regulatory compliance with capital measures at March 31, 2010. The two banks whose capital we have monitored most closely are FHLB-Pittsburgh and FHLB-Seattle due to the risk-based capital test. Both these banks remain in compliance with all of their regulatory capital requirements. Nevertheless, the Federal Housing Finance Agency, its regulator, still classifies FHLB-Seattle as "undercapitalized." We continue to monitor the regulatory

environment for the System, including important aspects of risk management and governance.

Overall, combined System assets were \$966 billion at March 31, 2010, a decrease of 5% from \$1.016 trillion at Dec. 31, 2009. Advances (secured loans to members) decreased 9% to \$572 billion and represented 59% of total assets at March 31, 2010. System advances continued to decline, albeit more slowly, due to weak loan demand from member banks. Effective and efficient alternative sources of liquidity in the capital markets have also continued to improve for member banks.

Finally, many member banks experienced deposit growth during the past two quarters, affording them excess liquidity since a weak economy and weak securities markets have made depositing cash in banks a conservative and safe option. We believe advances may decline at least through the next two quarters, specifically until a more robust economic recovery sparks commercial loan demand and liquidity needs at member banks.

In line with our expectation for weakness in the housing and mortgage sectors through 2010, we believe the FHLB System banks will record more, but manageable, OTTI in the remaining quarters of 2010. We believe that mortgage-related losses will continue to grow through 2010 as foreclosures settle but inventory levels remain high while sales volumes remain low, further pressuring home values. Private-label RMBS represented only about 5% of total system assets at March 31, 2010. The FHLB System banks recognized \$233 million of credit-related OTTI charges on certain private-label MBS during first-quarter 2010. This represents a 35% decrease from \$436 million of credit-related OTTI in fourth-quarter 2009 and a 55% decrease from the \$516 million of credit-related OTTI charges recorded in first-quarter 2009.

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