

Third Quarter Call Report Trends

November 18, 2020



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Presenters



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Overview

- Interest Rates and the Economy
- Call Report Trends
- Balance Sheet Strategies

Interest Rates and the Economy



Interest Rates and the Economy

- Short- and Long-Term Rates
- Mortgage Market Conditions
- Economic Trends

Change in Short-Term Yields

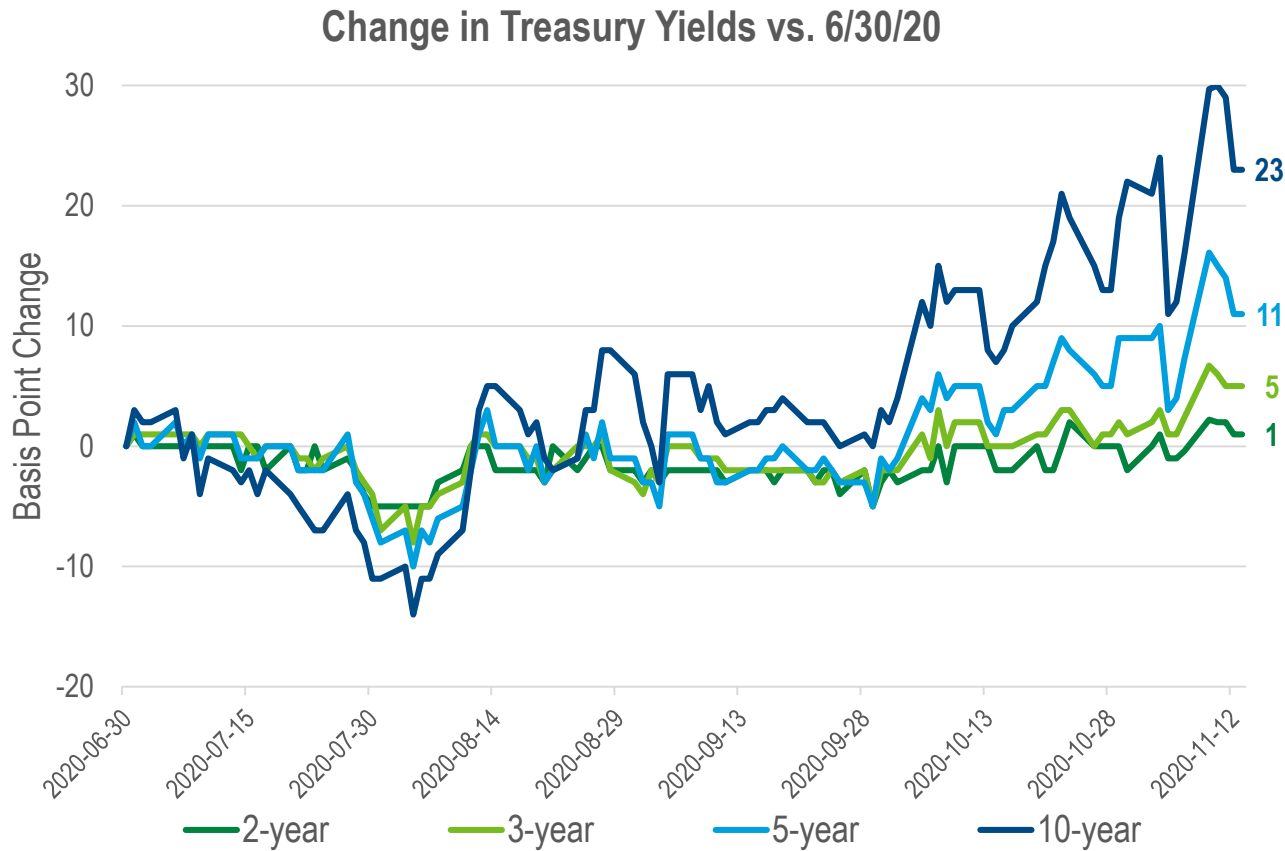
In keeping with Fed guidance, short-term rates haven't moved higher

	1-Month Treasury	3-Month Treasury	6-Month Treasury	12-Month Treasury	SOFR	Fed Funds	1-Month LIBOR	3-Month LIBOR
6/30/2020	0.13%	0.16%	0.18%	0.16%	0.10%	0.08%	0.16%	0.30%
7/31/2020	0.09%	0.09%	0.10%	0.11%	0.10%	0.10%	0.15%	0.25%
8/31/2020	0.08%	0.11%	0.13%	0.12%	0.11%	0.09%	0.16%	0.24%
9/30/2020	0.08%	0.10%	0.11%	0.12%	0.08%	0.09%	0.15%	0.23%
10/31/2020	0.08%	0.09%	0.11%	0.13%	0.09%	0.09%	0.15%	0.21%
11/12/2020	0.09%	0.09%	0.11%	0.13%	0.10%	0.09%	0.14%	0.22%
November vs. June	-0.04%	-0.07%	-0.07%	-0.03%	0%	+0.01%	-0.02%	-0.08%

Source: Federal Reserve Bank of St. Louis

Change in Long-Term Yields

However, the intermediate and long end of the yield curve has steepened

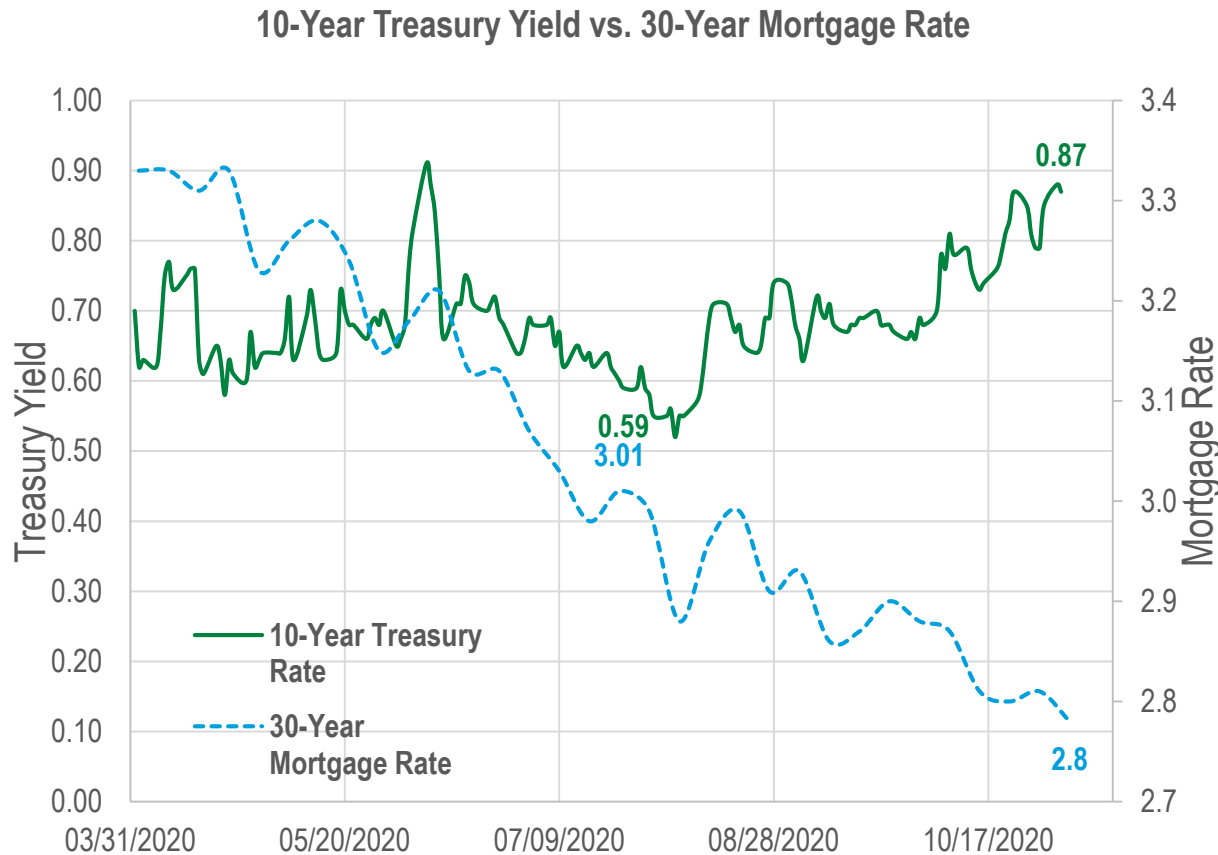


- Longer rates have risen by 20-40 basis points vs. early August lows
- Post-election flattening erased some of that shift
- Vaccine news resumed the trend higher
- Impact on asset yields?

Source: Federal Reserve Bank of St. Louis, FHLBank Boston

Mortgage Rates

Despite higher Treasury yields, mortgage rates have moved lower

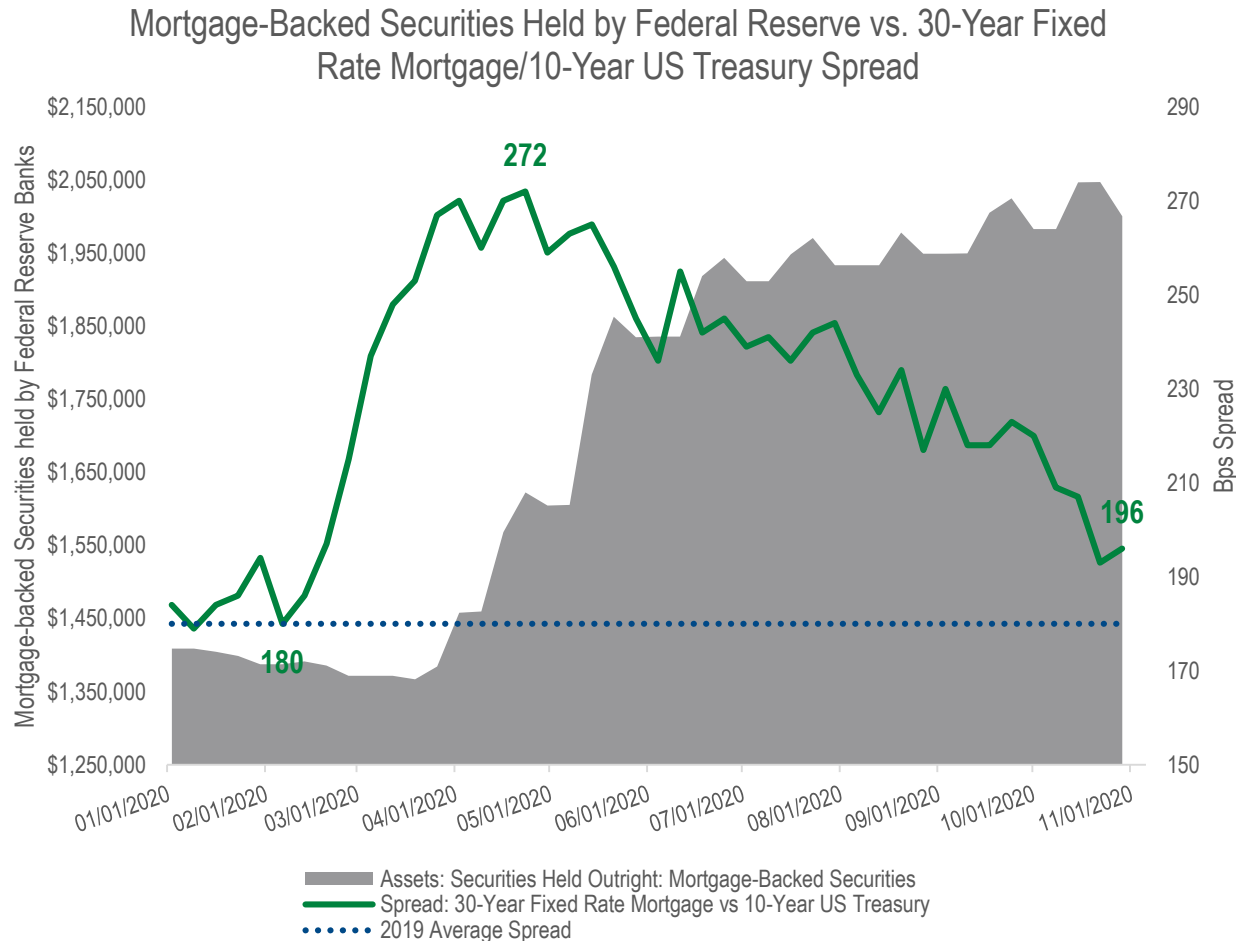


- Mortgages broke through 3% even as the long end of the Treasury curve weakened
- Historically wide spreads allowed for long-duration fixed-rate asset to *appreciate* in price even as yields moved higher

Source: Federal Reserve Bank of St. Louis, FHLBank Boston

Mortgage Spreads

Fed support of MBS market has kept spreads tight despite elevated prepayment risk

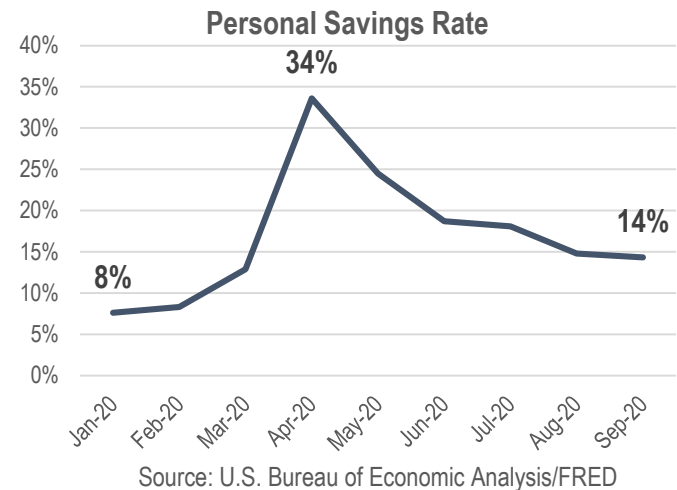
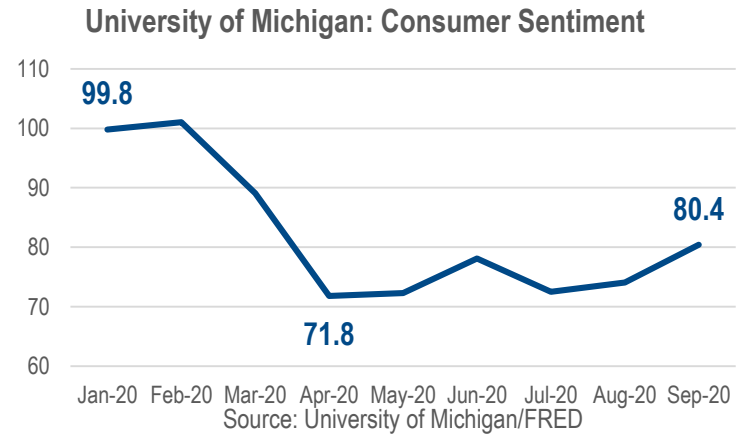
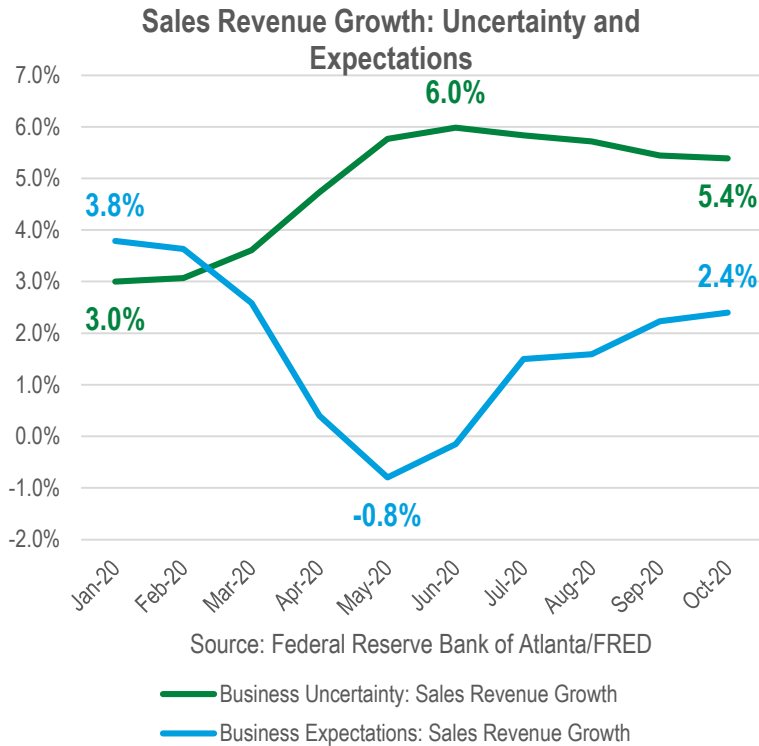


- Portfolio has grown by ~\$600 billion, even as paydowns accelerated
- ~75 bps of tightening for loan spreads, but still above historical average
- Originators are rebuilding capacity; catalyst for further rate declines?

Source: Federal Reserve Bank of St. Louis, FHLBank Boston

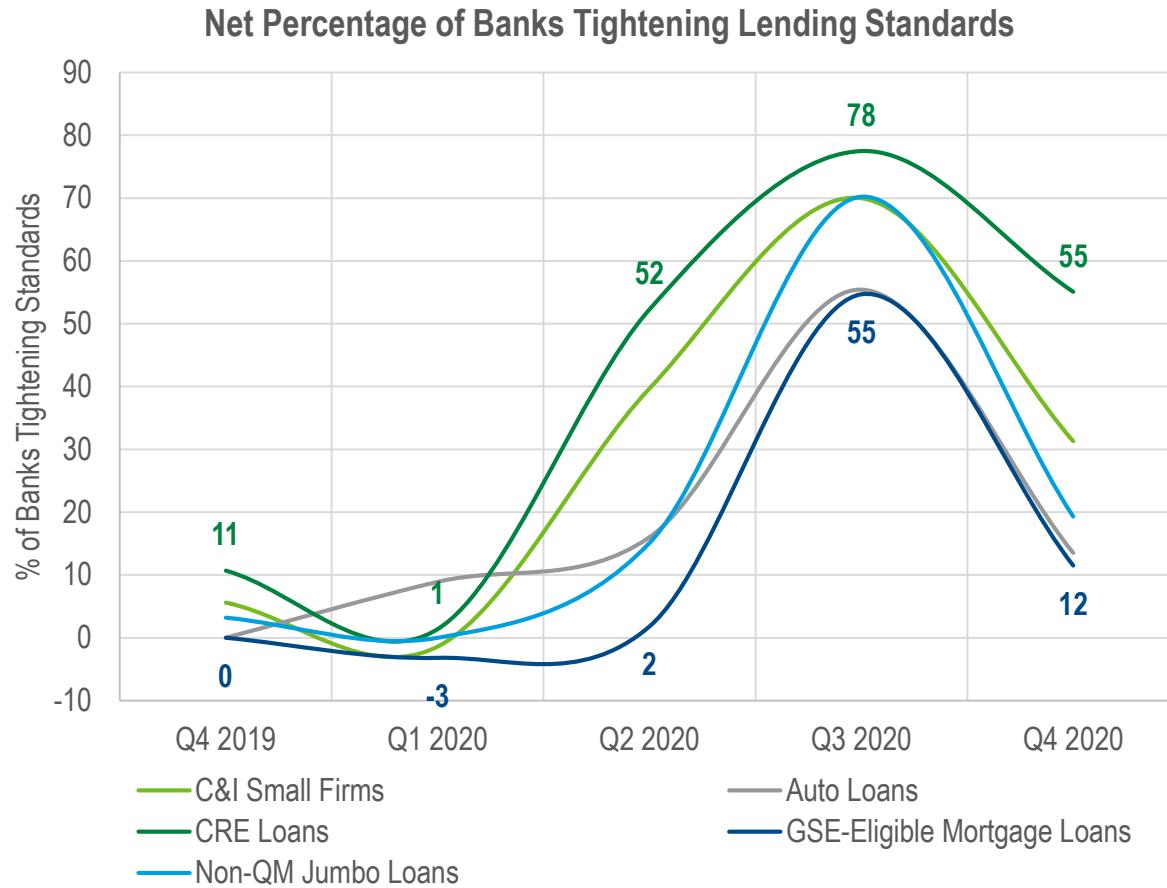
Economic Data

In uncharted waters, mixed signals on the health of the consumer and businesses



Lending Standards

According to Fed's Senior Lender Survey, access to credit is loosening



- Typically, 10-20% is seen as a big move and an indicator of a shift in sentiment
- Improvements across all types, but more recovery for the consumer (mortgage, auto) vs. commercial (C&I, CRE)

Source: Federal Reserve Bank of St. Louis

Call Report Trends



Call Report Trends

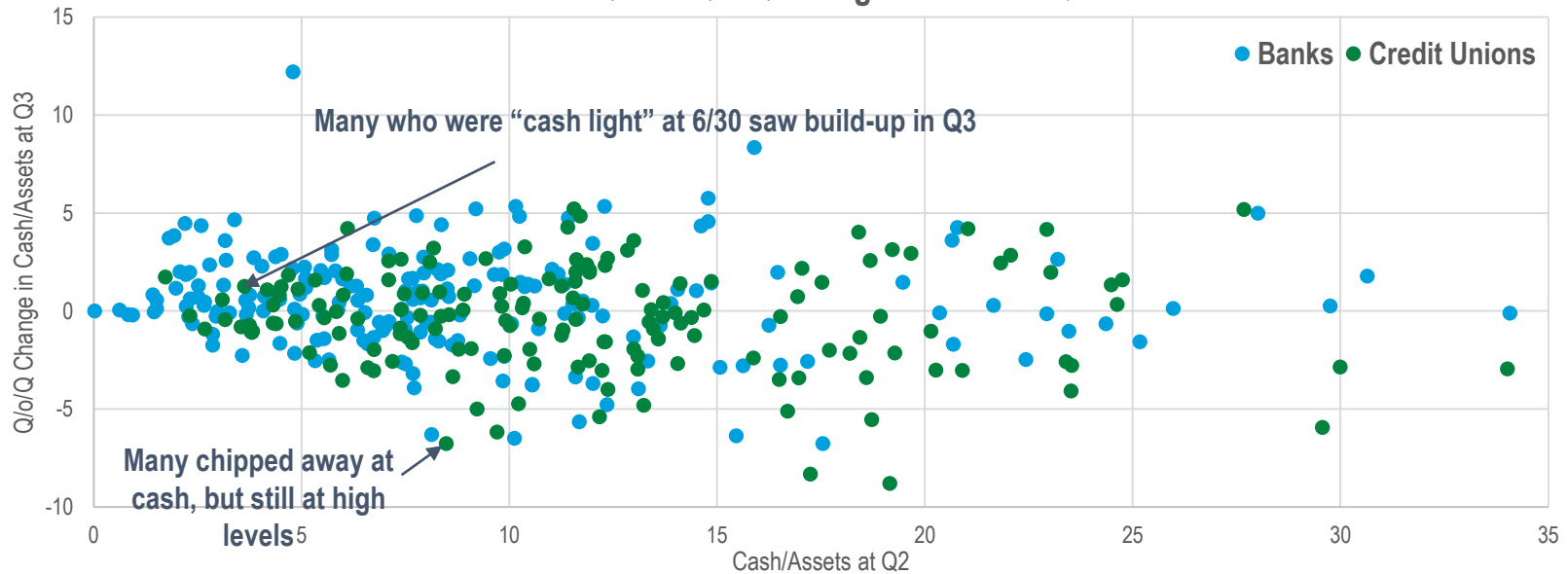
- Liquidity
- Yields and Margin
- Funding Mix
- Industry Outlook

Elevated Cash Levels

Driven by unprecedented deposit flows, tepid loan growth, and record low investment yields

Member Type	Members with Cash >5% as of 12/31/19	Members with Cash >10% as of 12/31/19	Members with Cash >5% as of 9/30/20	Members with Cash >10% as of 9/30/20
Banks	27%	11%	68%	32%
Credit Unions	47%	15%	75%	45%

Cash at Q2 vs. Q/o/Q Change in Cash at Q3



Source: Call Report Data, FHLBank Boston

High Cash and High Performance?

Members can still produce above average ROA with a lot of cash- but the hurdles are higher

Member Type	Group	Return on Assets	Net Interest Margin	Non-Interest Income/Assets	Efficiency Ratio
Banks	>Median ROA + >10% Cash	0.97%	2.88%	0.78%	64%
	All other Banks	0.48%	2.91%	0.46%	78%
Credit Unions	>Median ROA + >10% Cash	0.81%	3.38%	1.31%	76%
	All other Credit Unions	0.12%	2.80%	0.60%	84%

- **Margin:** A differentiator for credit unions; (surprisingly) less so for banks
- **Fee Income:** Meaningful for banks and credit unions
- **Efficiency:** Greater impact with banks

Source: Call Report Data, FHLBank Boston

PPP Activity

Modest usage of the PPPLF; what will the timing for forgiveness be?

3/31 Metrics	PPPLF Users	Non-PPPLF Users
Loan/Deposit Ratio	100.02	94.75
Cash/Assets	3.06	4.24
Capital Ratio	10.38	11.27

PPPLF Usage (New England & National)	
Total PPP Loans	\$23.969 billion
PPPLF Outstanding	\$1.765 billion
PPPLF Usage Ratio (New England)	7.3%
PPPLF Usage Ratio (National)	16.8%

PPPLF Usage by Assets	
0-25 th percentile	8.57%
25-50 th percentile	20.83%
50-75 th percentile	10.42%
75-100 th percentile	22.92%

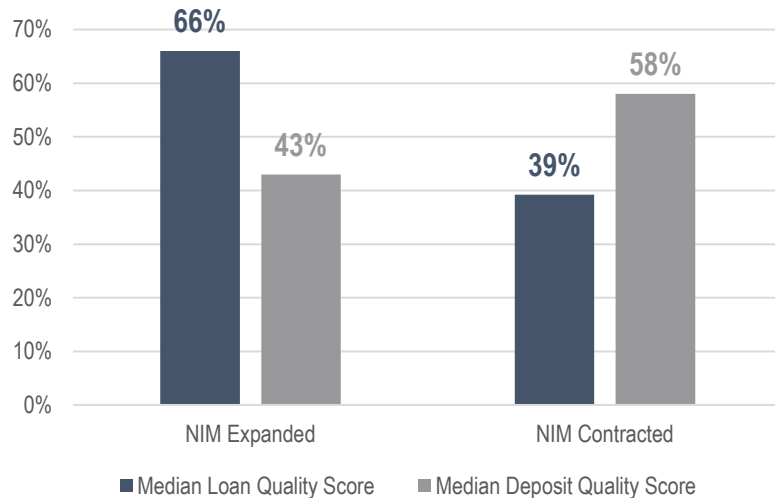
- PPP loans have largely been self-funded; large percentage of balances remain in checking accounts
- At a 1% rate, balances have been a cheap rainy-day fund for customers
- Forgiveness or not, 2021 or 2022, is the cash going to leave the institution?
- “Tsunami of liquidity” in accelerated scenarios, compounding current challenges posed by high cash levels

Source: Federal Reserve Bank of St. Louis, Call Report Data, FHLBank Boston

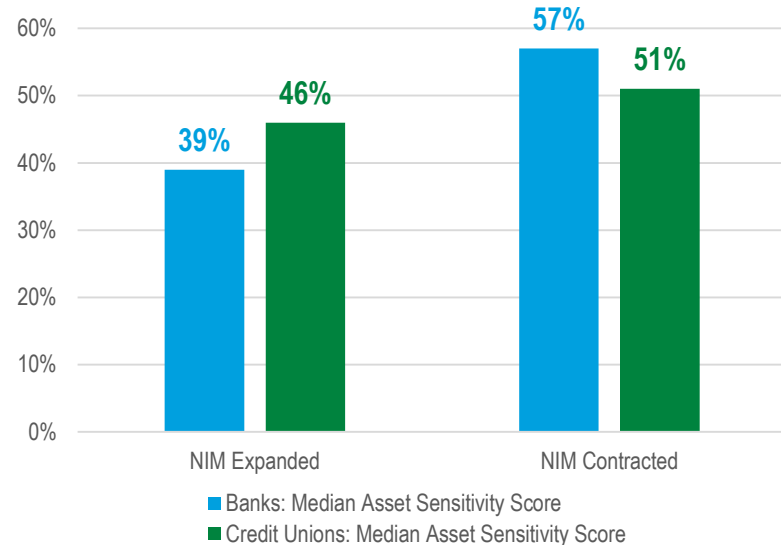
What is Driving Margins?

Margin expansion being driven by lending side, as opposed to funding and interest-rate risk

Loan and Deposit Quality Scores vs. Q3 NIM Change



Asset Sensitivity Score vs. Q3 NIM Change

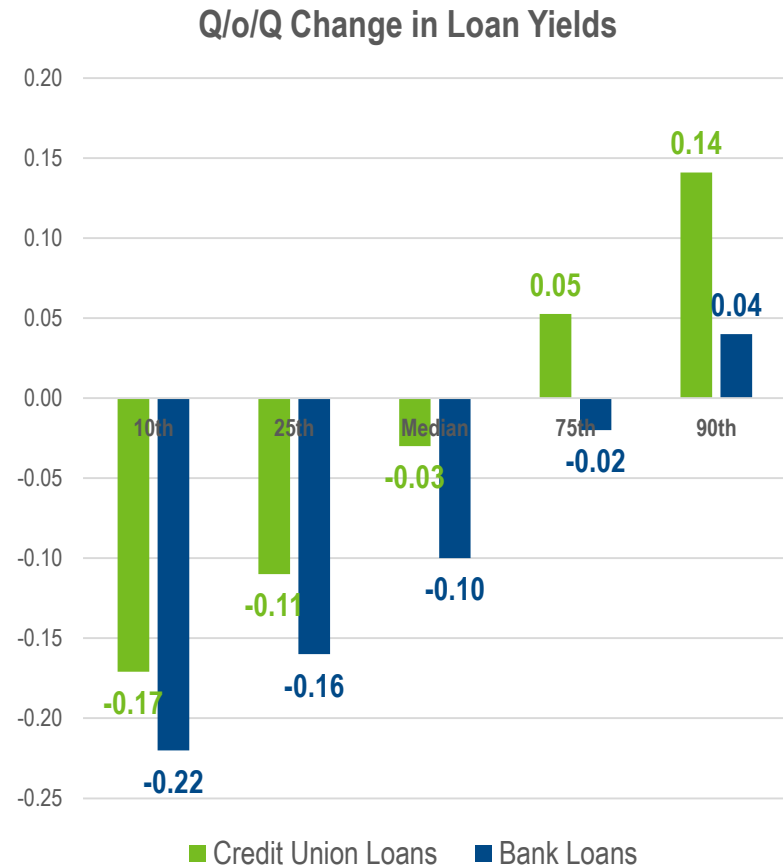
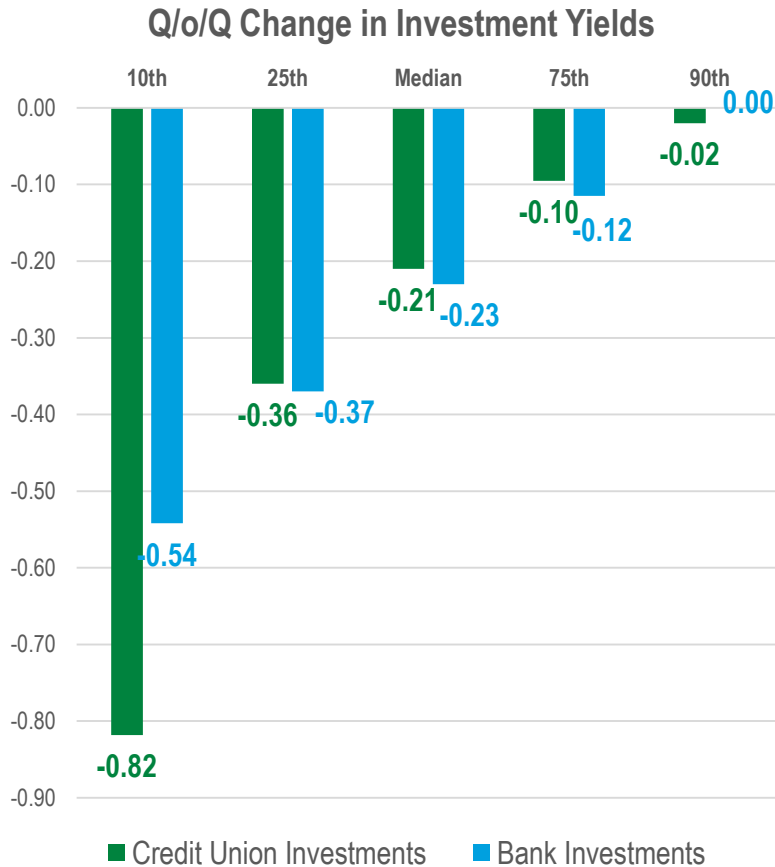


- **Loan Quality Score:** *Large impact*; loan/assets, yields, credit performance
- **Deposit Quality Score:** *Minimal impact*; core funding, deposit mix and cost
- **Asset Sensitivity Score:** *Modest impact*; loan/deposit mix, repricing gap

Source: Call Report Data, FHLBank Boston

Changes in Yields

Asset yield pressures continue; elevated cash and prepay pick-up create additional pressure

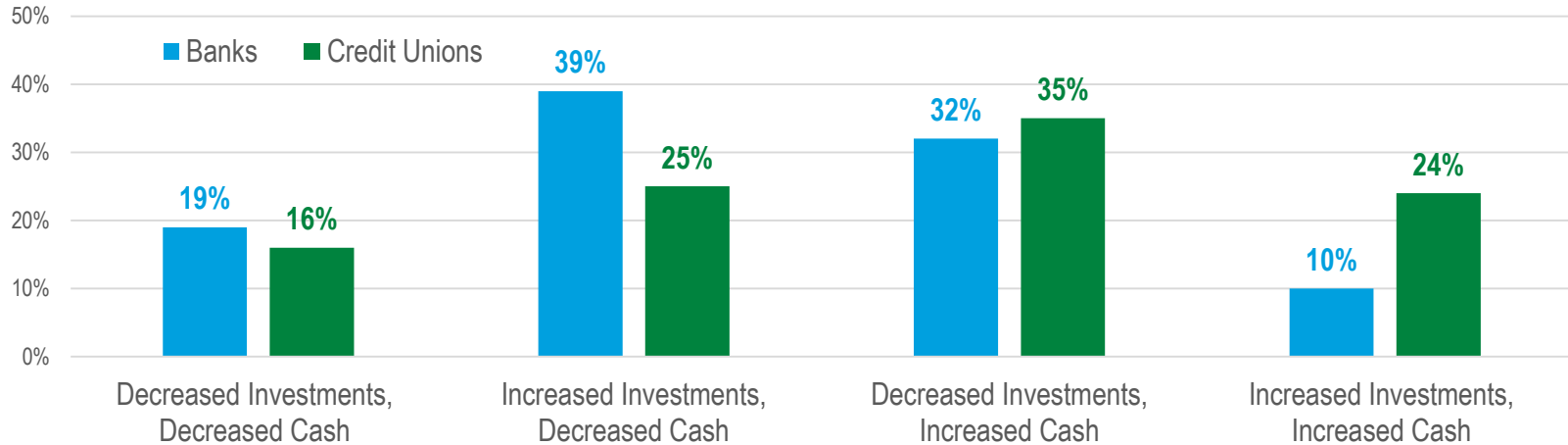


Source: Call Report Data, FHLBank Boston

Investing Excess Liquidity

Mixed results on effectiveness of working down cash levels

Q/o/Q Change in Investments and Cash



Liquidity -> Loans

Cash -> Investments

Investments -> Cash

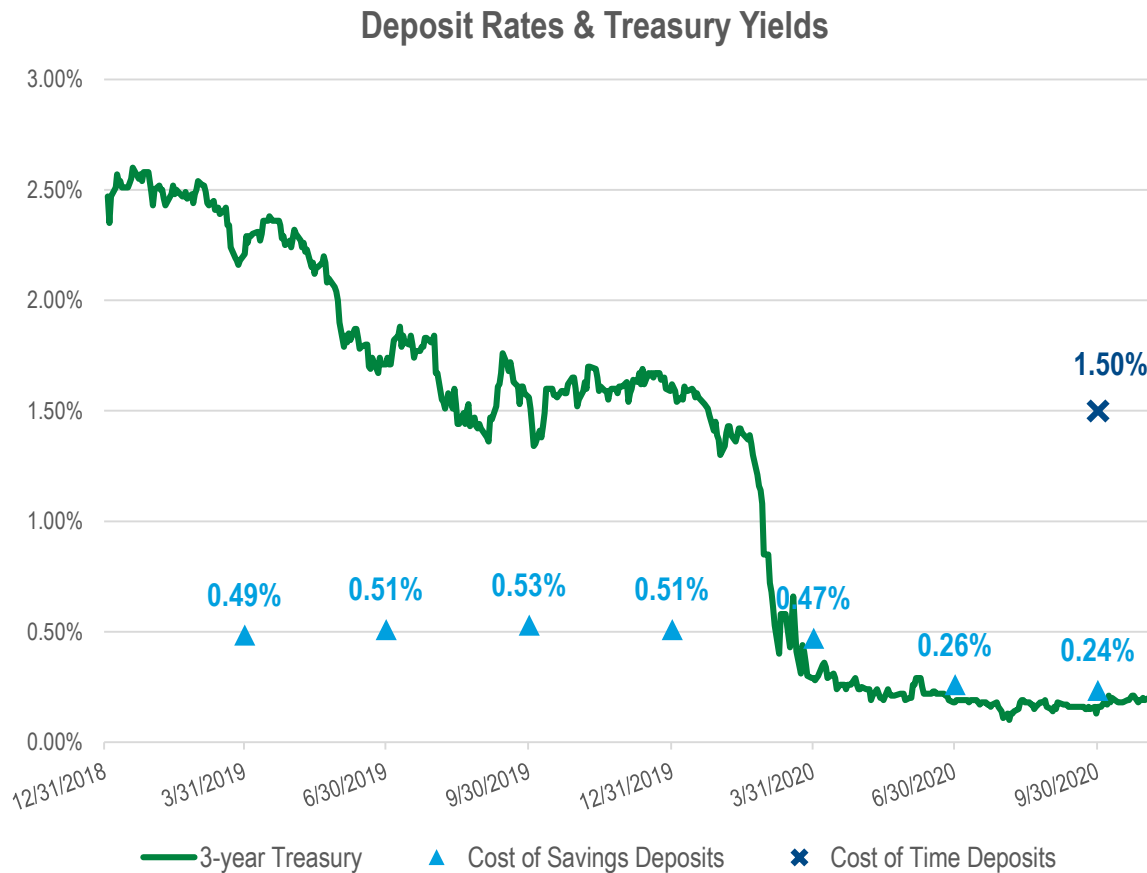
Loans -> Liquidity

- Under 20% were able to direct excess liquidity into loans
- **Banks:** Slight shift from cash to investments
- **Credit Unions:** Slight shift from investments to cash
- Impact of short duration and high prepayment and call risk

Source: Call Report Data, FHLBank Boston

Deposit Rates

At current level of wholesale rates, value of sticky, low-cost deposits is diminished

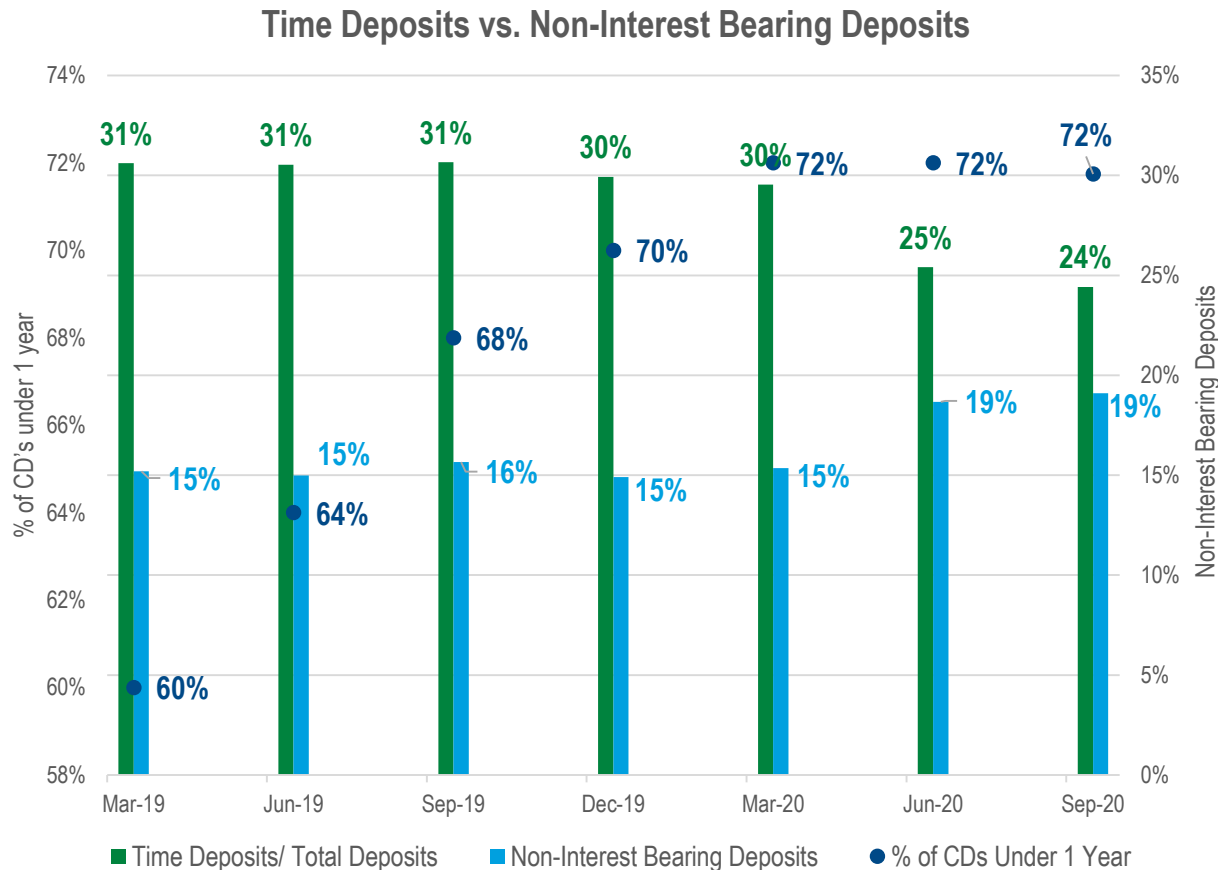


- Through 2019, rate paid on savings accounts were 100-200 bps below that of the 3-year Treasury rate; now deposit rates are higher
- There is still significant room for cost of funds savings in term deposits, in absolute and relative terms

Source: Call Report Data, Federal Reserve Bank of St. Louis, FHLBank Boston

Deposit Mix

At current level of wholesale rates, value of sticky, low-cost deposits is diminished



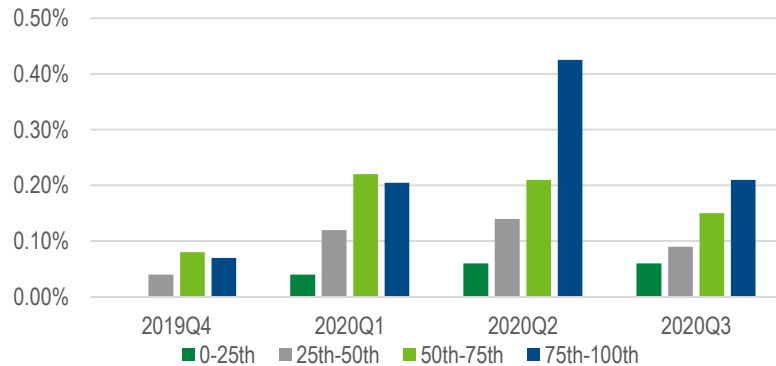
Source: Call Report Data, FHLBank Boston

- As rates have fallen, reliance on term deposits has decreased
- Average life has been trending shorter, with 72% repricing inside of 1 year
- Repricing frequency helps in **declining rate environment**- but what about in a **volatile liquidity environment**?

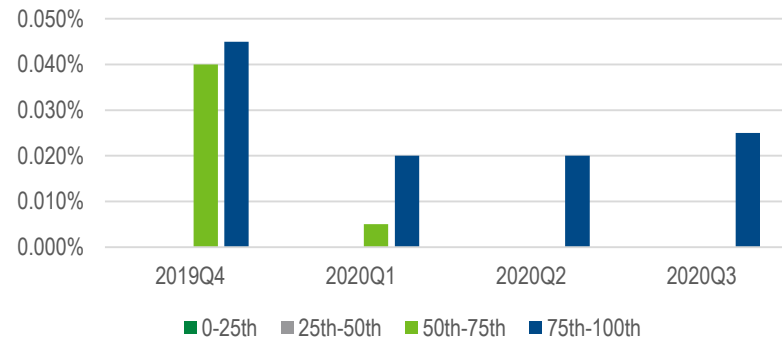
Credit Performance

Provisions down, NPAs and NCOs unchanged; NCO outliers more reliant on C&I

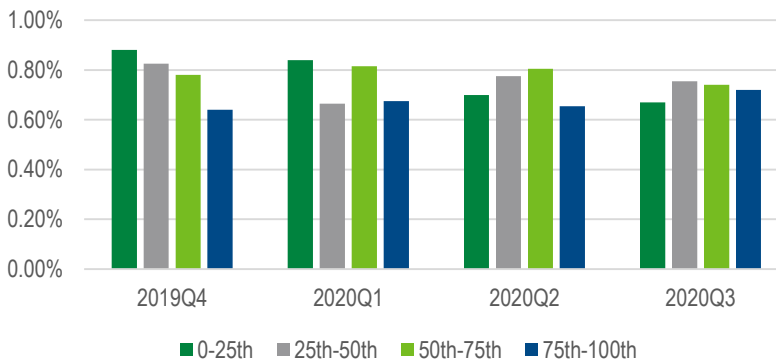
Median Provision Expense, by Asset Size Percentile



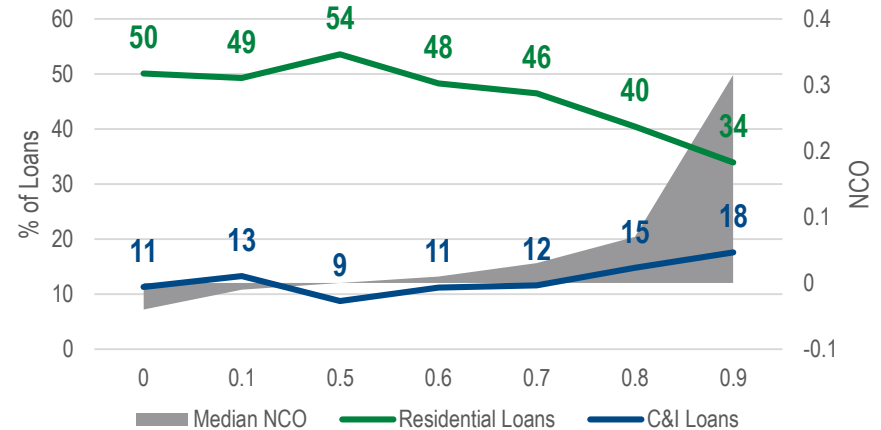
Median Net Chargeoffs, by Asset Size Percentile



Median NPAs/Loans, by Asset Size Percentile



Loan Composition, by NCO Percentiles

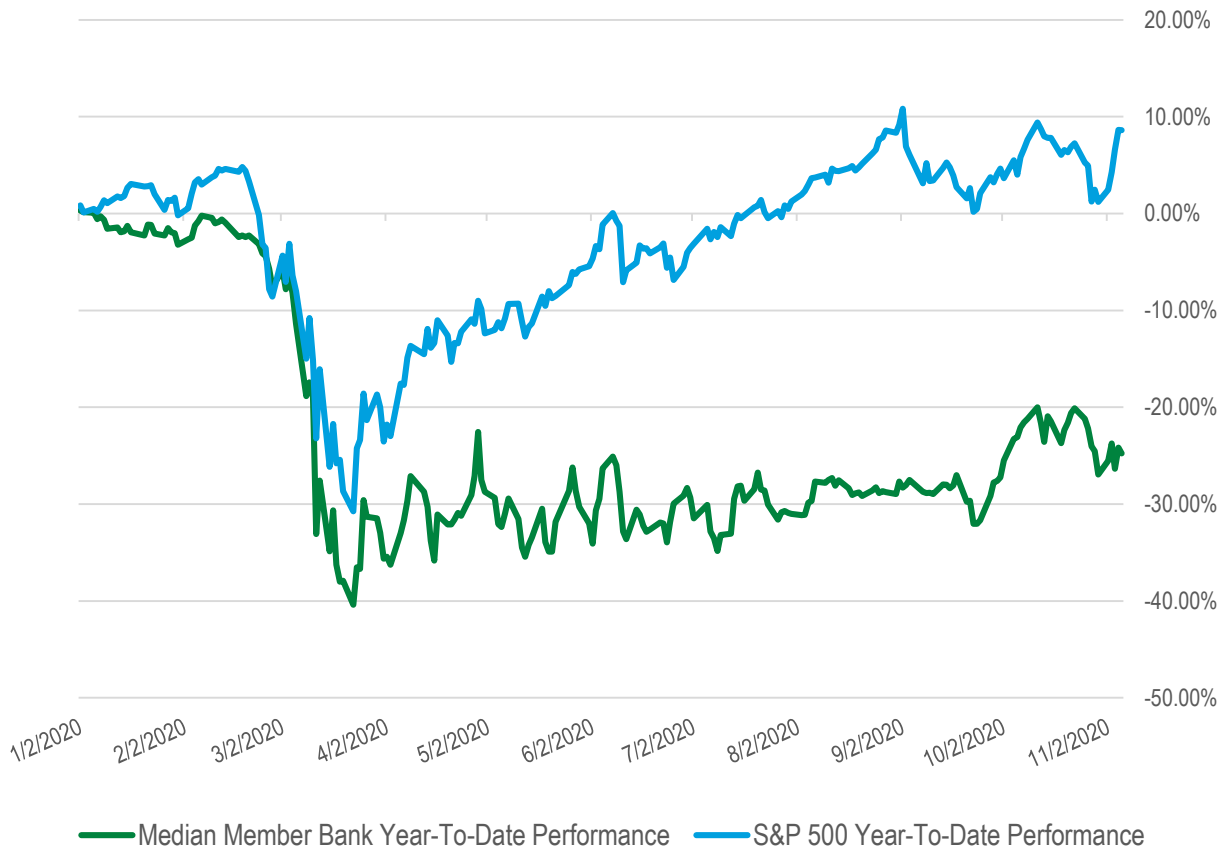


Source: Call Report Data, FHLBank Boston

Public Bank Performance

Bank stocks were hit harder at the onset of the pandemic, and have been slower to recover

Year-To-Date Performance



YTD Performance (through 11/6)	
Median Member Bank	-25%
KBW Regional Bank ETF	-27%
S&P 500	+9%

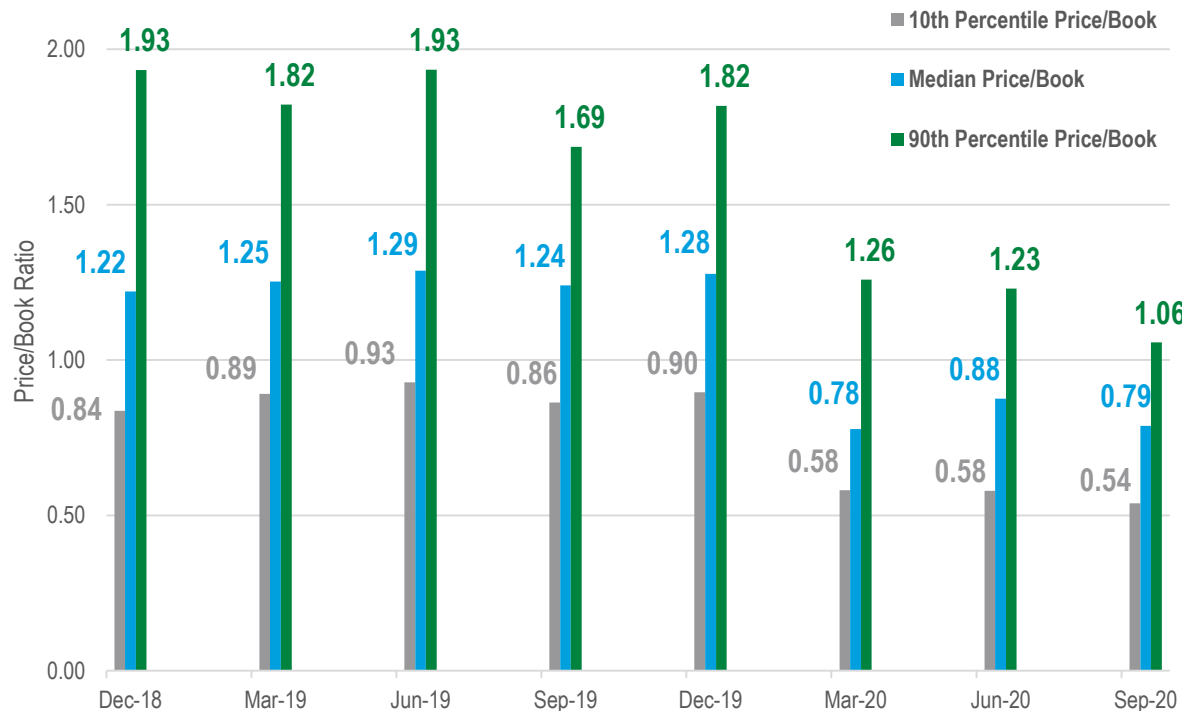
YTD Performance (through 11/6)	
10 th Percentile	-43%
25 th Percentile	-38%
Median	-25%
75 th Percentile	-12%
90 th Percentile	-1%

Source: S&P Global, FHLBank Boston

Valuation Looking Forward

Low interest-rate environment and credit uncertainty leading to softer multiples

Price/Book Ratio: FHLBank Boston Public Members



Source: S&P Global, FHLBank Boston

- Even through the flattening of the yield curve in 2019, price/book ratios held firm
- Uncertainty around the level of future earnings has led to prices below book value

Balance Sheet Strategies

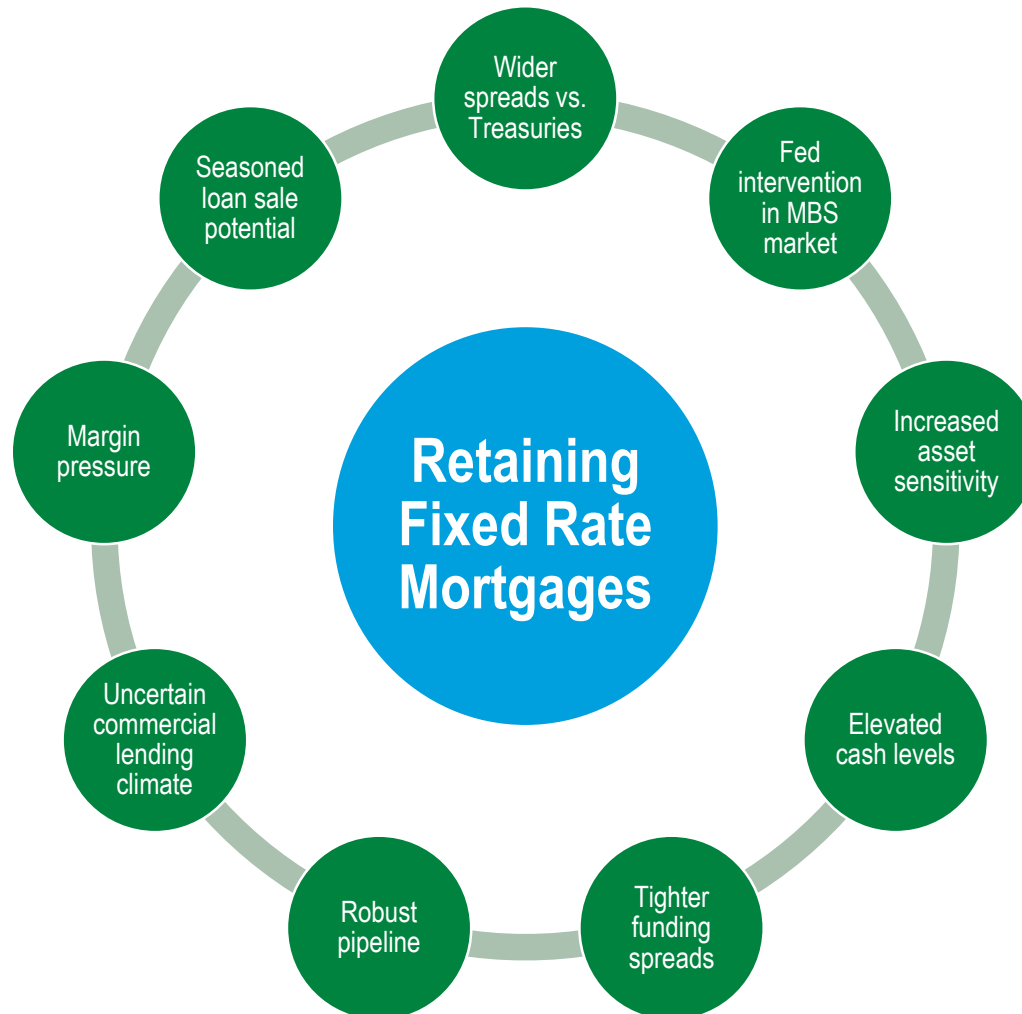


Balance Sheet Strategies

- Deploying Excess Liquidity
- Reducing Cost of Funds
- Value in Term Floaters

Deploying Excess Liquidity

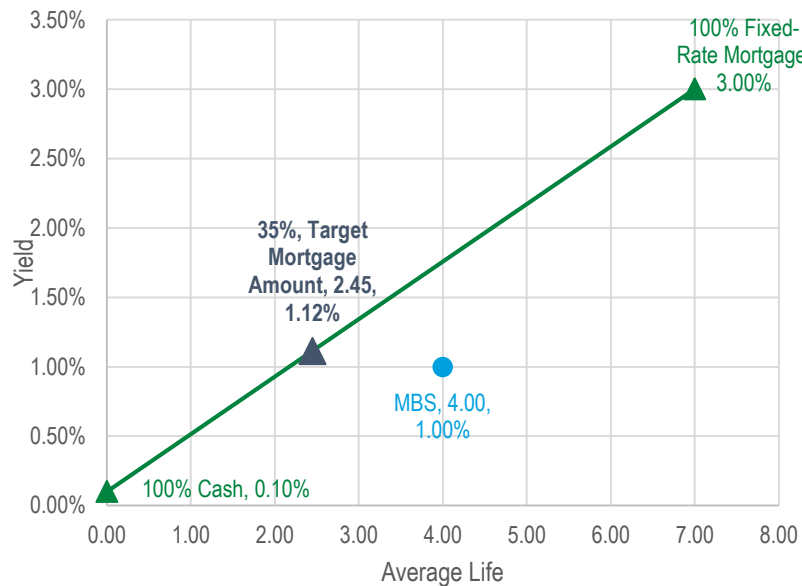
Market conditions and balance sheet profiles are now more supportive of holding mortgages



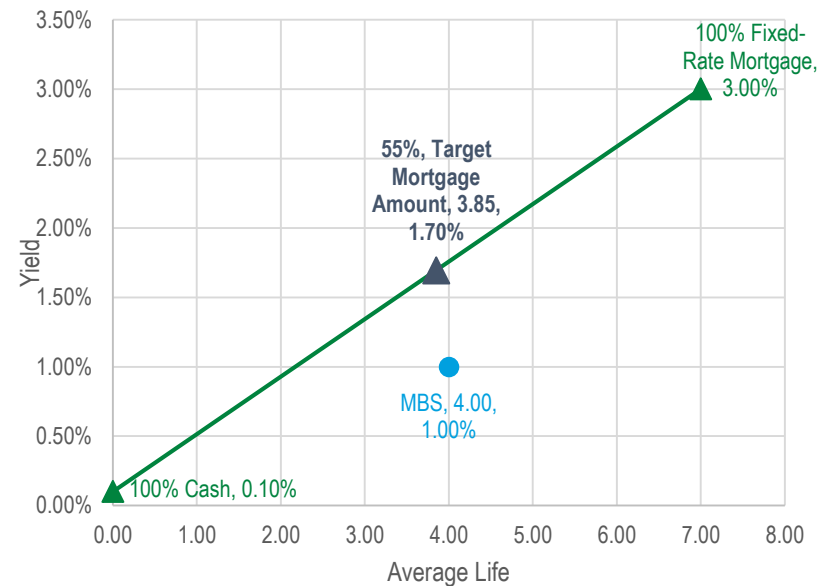
Deploying Excess Liquidity

Cash and mortgage barbell can be an alternative to unappealing investment options

Mortgage/Cash Barbell vs. MBS



Mortgage/Cash Barbell vs. MBS



Comparable yield vs. securities

35% Mortgages/65% Cash

Shorter average life by ~1.5 years

Comparable average life vs. securities

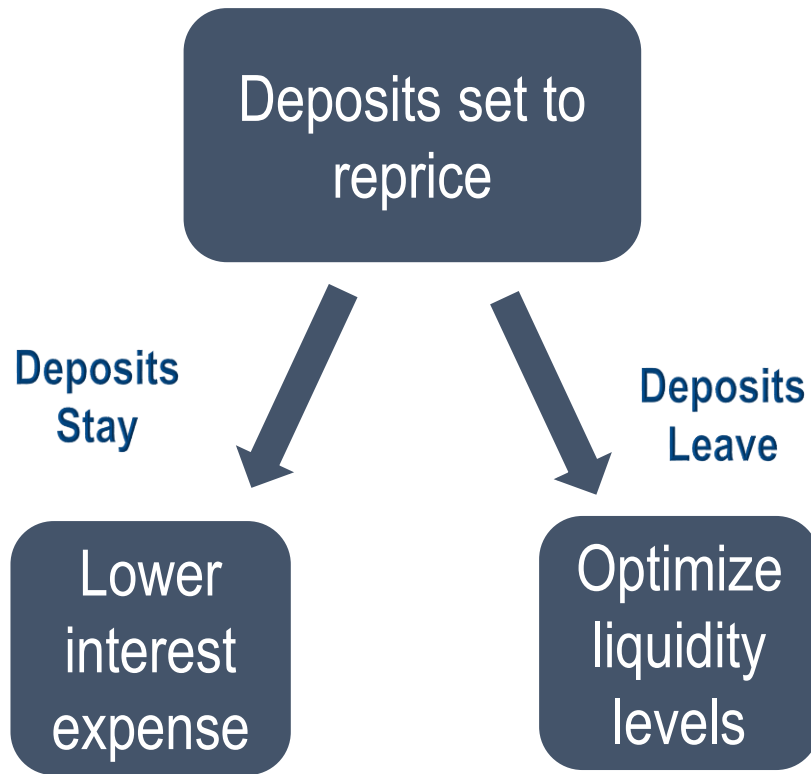
55% Mortgages/45% Cash

0.70% more yield

Source: FHLBank Boston

Reducing Cost of Funds

Turn your excess liquidity position from challenge to opportunity, to combat margin pressures



Credit Unions	4Q 2019	3Q 2020	Change
Loan/Deposit	89.33	78.34	-10.99
Cash/Assets	5.80	10.73	+4.93
NIM	3.47	3.17	-0.30

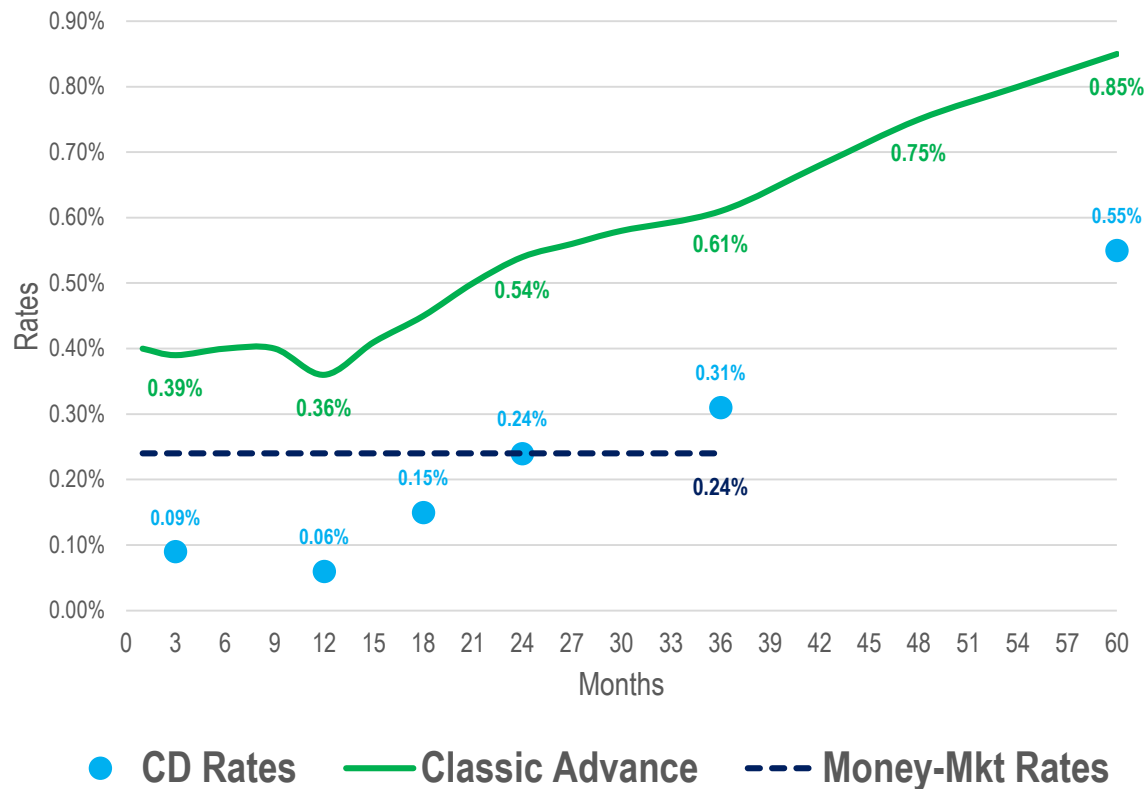
Banks	4Q 2019	3Q 2020	Change
Loan/Deposit	98.23	91.43	-6.80
Cash/Assets	4.01	7.55	+3.54
NIM	3.21	3.02	-0.19

Source: Call Reports, FHLBank Boston

Reducing Cost of Funds

Market conditions and balance sheet profiles are now more supportive of holding mortgages

Deposit Rates vs. Advances

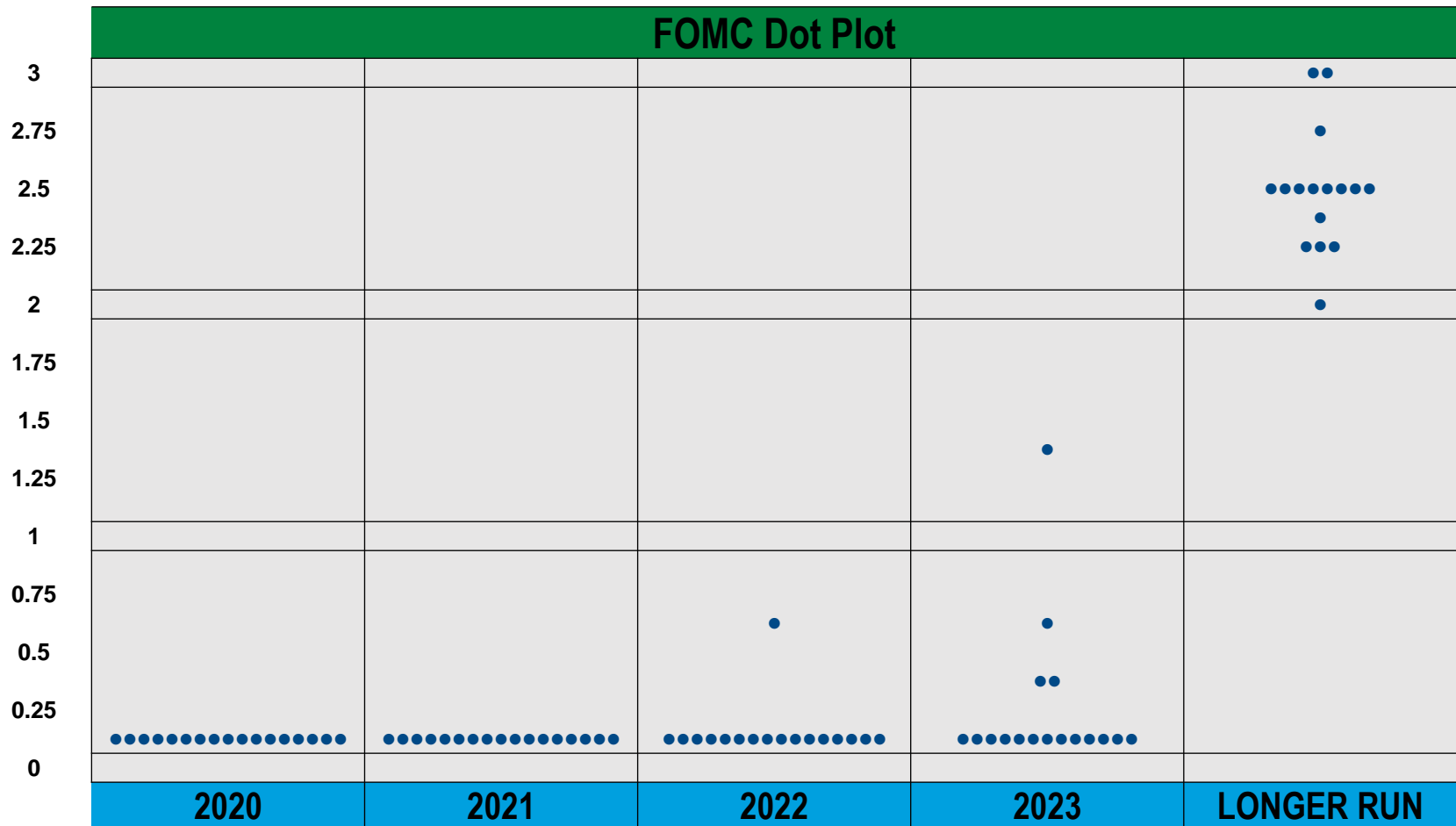


Source: FHLBank Boston

- If **75-90%** of your:
 - maturing CDs rolled at **advances less 0.30%**
 - Money markets priced at **Fed Funds plus 0.15%**
- Would that help your:
 - Earnings?
 - Liquidity?
 - Interest-rate risk?
- After shifting short, is it time to incent longer?
 - Might not work, but it could help ease liquidity challenges

Value in Term Floaters

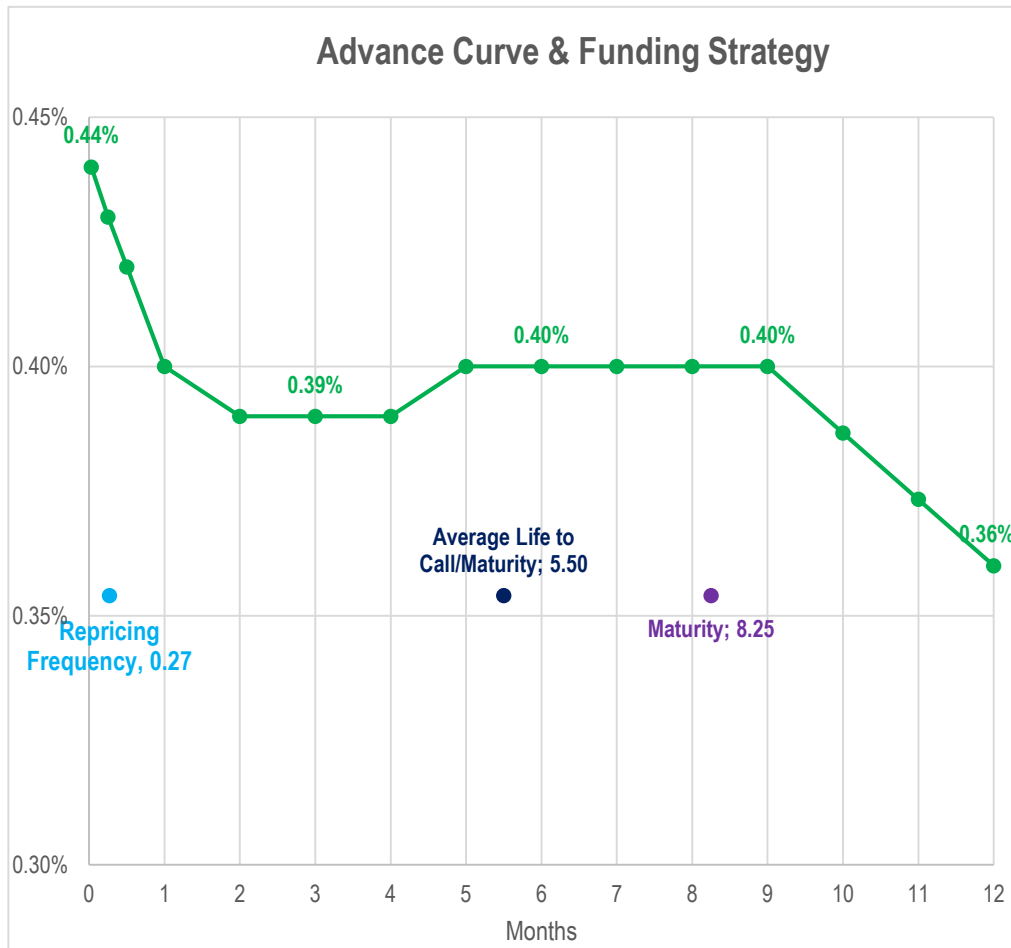
Fed indications are that **short-term** rates aren't going higher; less certainty further out the curve



Source: Federal Reserve

Value in Term Floaters

Align funding duration with Fed guidance; but reduce cost and minimize spread volatility risk



Advance Type	Amount	Initial Rate
3-month SOFR-Indexed Advance	25%	0.31%
6-month SOFR-Indexed Advance	25%	0.33%
12-month SOFR-Indexed Advance	25%	0.36%
1-year/1-month DNA-Floater Advance	25%	0.42%
TOTAL		0.35%

- 2-9 bps cheaper than Short-Term Classic Advances
- Weighted repricing frequency of a little over one week
- **Maturity** of a little over 8 months
- **Average life to call** of 5.5 months

Source: FHLBank Boston

Thank You

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