Discussion Overview

- US and New Mexico economic trends
- US banking industry trends
- How do New Mexico banks compare?
- Post recession status of the FHLBanks
- Current state of the FHLBank of Dallas
- Looking Forward: Regulatory, housing finance, and GSE reform
- Q&A
US Economic Conditions

- Economic conditions are improving but still generally slower than expected
  - GDP growth is moderate but positive
  - Unemployment rates are declining at a slow but steady pace
  - Housing markets are now contributing to economic growth

- Federal Reserve is expected to continue its extremely accommodative policy for the near term but there is some dissension on the Board
  - Unemployment is improving but still higher than target while inflation remains subdued
  - Speculation about the Fed’s unwind has caused recent market volatility

Percentage Change in Real GDP: Mixed performance across states—New Mexico GDP growth below U.S. average in 2012

Source: U.S. Bureau of Economic Analysis
US economic conditions improving driven in part by the improving housing market, but conditions still far from normal.

Source: U.S. Census Bureau

Housing market conditions are improving across many parts of US; housing prices in New Mexico have been relatively flat over the last 2 years.

Source: FHFA Home Price Index

Source: U.S. Census Bureau

Source: FHFA Home Price Index
Unemployment rates lower in 4 of 5 Dallas District states compared to US; after slowly trending down, New Mexico unemployment rates have flattened in 2013.

Monthly Unemployment Rates, Seasonally Adjusted:
May 2007 – May 2013

Source: Bureau of Labor Statistics

NM Unemployment Rates, Not Seasonally Adjusted: unemployment rates peaked in 2010 and have slowly improved across many counties.

Unemployment rates by county, 2006
Unemployment rates by county, 2010
Unemployment rates by county, 2011
Unemployment rates by county, May 2013

Source: Bureau of Labor Statistics
Government, education and health services industries are key drivers of employment in New Mexico.

Source: FDIC Website

Industry profitability has significantly improved while concerns about NIM pressure and subdued loan demand persist.

- **Profitability**
  - Industry profitability improving driven in part by lower provision expense
  - Low rates are putting pressure on net interest margins and moderating profit improvement

- **Asset Quality**
  - Gradually improving but non-performing loans remain higher than historical norms

- **Asset / Loan Growth**
  - Although annual loan growth has been modest, generally stronger growth in 2011 and 2012

- **Asset / Liability Mix**
  - Cash & securities comprise a greater percentage of the balance sheet in 2012 compared to historical norms due to weak loan growth vs. strong deposit growth
  - Deposit growth continued to outpace loan growth

Number Employed and Percent of Total Employment

QECA = Not Seasonally Adjusted
Source: Bureau of Labor Statistics (BLS) / Haver Analytics
Data Updated: 20/09/2015
**Industry Consolidation:** After peaking in 2010, bank failures have significantly declined, merger activity remains relatively modest, but deals have increased.

**Banks & Thrifts: New Charters, Bank Mergers & Bank Failures, 2007 – 2012, 1Q13**

- **New Charters:**
  - 2007: 100
  - 2008: 150
  - 2009: 200
  - 2010: 250
  - 2011: 300
  - 2012: 350
  - 1Q13: 400

- **Bank Mergers:**
  - 2007: 50
  - 2008: 100
  - 2009: 150
  - 2010: 200
  - 2011: 250
  - 2012: 300
  - 1Q13: 350

- **Bank Failures:**
  - 2007: 10
  - 2008: 20
  - 2009: 30
  - 2010: 40
  - 2011: 50
  - 2012: 60
  - 1Q13: 70

*Source: FDIC Quarterly Banking Profiles and Graph Books*

456 banks & thrifts have failed since 2009, including 3 in NM; failures concentrated in Southeast, Midwest and West Coast.

*Source: SNL, As of June 28, 2013*
Industry profitability continued to improve, although ROE remained below 2004–06 levels; declines in loss provision have boosted profitability since 2009, while NIM pressures impacted institutions of all sizes.

Source: FDIC Quarterly Banking Profile Graph Book

Profitability strongest on the west coast and Midwest; most Dallas District states ranked amongst top 25 performing states, including New Mexico.

Source: FDIC Quarterly Banking Profile Graph Book
Largest institutions hurt most during recession and improved the most; national non-performing loan ratios declining across asset size groups

New Mexico Banking Industry Changes: 2008 vs. 1Q 2013
and New Mexico Credit Unions at 1Q13

<table>
<thead>
<tr>
<th>New Mexico Banks &amp; Thrifts</th>
<th>NM Credit Unions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>1Q 2013</td>
</tr>
<tr>
<td>Number</td>
<td>53</td>
</tr>
<tr>
<td>Total Assets</td>
<td>$16,696 mm</td>
</tr>
<tr>
<td>Employees</td>
<td>4,452</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Bank Failure</th>
<th>City</th>
<th>ST</th>
<th>Acquiring Institution</th>
<th>Closing Date</th>
</tr>
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<tbody>
<tr>
<td>First Community Bank</td>
<td>Taos</td>
<td>NM</td>
<td>U.S. Bank, N.A.</td>
<td>28-Jan-11</td>
</tr>
<tr>
<td>High Desert State Bank</td>
<td>Albuquerque</td>
<td>NM</td>
<td>First American Bank</td>
<td>25-Jun-10</td>
</tr>
<tr>
<td>Charter Bank</td>
<td>Santa Fe</td>
<td>NM</td>
<td>Beal Financial</td>
<td>22-Jan-10</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Major Charter Changes / Mergers</th>
<th>Acquirer / Charter Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of Albuquerque, NA</td>
<td>Bank of Oklahoma</td>
</tr>
<tr>
<td>Charter Bank (Beal)</td>
<td>Washington Federal</td>
</tr>
</tbody>
</table>

Source: FDIC website, FIRE
New Mexico banks & thrifts outperformed national community banks, although gap has narrowed

Median ROE: New Mexico vs. US Banks & Thrifts

![Median ROE graph]

Source: FIRE

Although low interest rates are putting downward pressure on margins, New Mexico community banks hold a spread advantage compared to peers

Median NIM* for New Mexico vs. US Banks & Thrifts

![Median NIM graph]

Source: FIRE

* Tax Equivalent
New Mexico’s median loss provision as a percentage of total assets was consistently better than US peers but improvements moderated in 2012.

**Median Loss Provision / Total Assets: New Mexico vs. US Banks & Thrifts**

New Mexico’s nonperforming loan ratios are similar to national peers, although New Mexico’s NPL ratios are increasing in 3 of 4 categories.

**Aggregate Non-performing Loans / Total Domestic Loans: NM vs. US Banks & Thrifts**
Loan Composition as of 1Q 2013:
New Mexico Banks & Thrifts vs. New Mexico Credit Unions

<table>
<thead>
<tr>
<th>Loan Type</th>
<th>NM Banks &amp; Thrifts</th>
<th>NM Credit Unions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Dollars in Millions</td>
<td>Dollars in Millions</td>
</tr>
<tr>
<td>Res/R/E</td>
<td>$2,200</td>
<td>$2,500</td>
</tr>
<tr>
<td>Constr &amp; Land Dev</td>
<td>$1,000</td>
<td>$1,500</td>
</tr>
<tr>
<td>Agri &amp; Farm</td>
<td>$100</td>
<td>$500</td>
</tr>
<tr>
<td>Comm &amp; Ind</td>
<td>$500</td>
<td>$0</td>
</tr>
<tr>
<td>Consumer</td>
<td>$500</td>
<td>$2,000</td>
</tr>
<tr>
<td>All Other</td>
<td>$1,000</td>
<td>$0</td>
</tr>
</tbody>
</table>

Source: FIRE

Loan growth rates have been subdued but are improving;
New Mexico banks & thrifts’ loan growth negative last three years

Aggregate Annual Loan & Lease Growth Rates: 2008 – 2012
New Mexico vs. US Banks & Thrifts

Source: FIRE
Post-Recession Status of FHLBanks

- System advances have shrunk by more than half since 2008 and by one-third from pre-crisis levels but have flattened since 4Q11.

- Despite reduced advances levels, profitability was up over 60 percent in 2012 over 2011.

- OTTI credit losses have dropped significantly—from $2.4 billion in 2009 to $113 million in 2012.

- FHLBanks’ exposure to PLMBS has declined by more than 65 percent since 2008.

- FHLBanks are well capitalized and have increased retained earnings by more than 260 percent since 2008.

FHLB System Advances increased over 50% during the credit crisis and subsequently declined due to increased member liquidity and lower loan demand; FHLB System advances relatively stable since mid-2011.
Similarly, FHLB Dallas advances peaked in 2008, providing members with much needed liquidity during the credit crisis, and have declined since then.

Core deposit growth at Dallas member community banks consistently exceeded loan growth the last five years by a significant margin, contributing to advances decline.
Many interrelated factors impact advances growth

**Member Status**
- Member Failures
- Member Financial Condition
- Membership Growth
- Mergers & Acquisitions

**Regulatory Environment**
- Financial Industry Regulation
- Regulatory Reform Legislation
- Regulatory Focus
- Political Climate

**Economic Conditions**
- Financial Markets
- Real Estate Trends
- Loan Demand & Business Growth
- Unemployment & Consumer Spending

**Competition**
- Wholesale Funding
- Core Deposits
- Government Programs
- Other GSEs

**Advances Growth**

### State of the FHLBank of Dallas

**Key Indicators**

- Advances stabilizing
  - Advances have declined about 75% from 4Q08 but have been relatively stable since mid-2011

- Earnings above historical averages
  - Above average returns since 2009 allowed Bank to further strengthen retained earnings by almost 175% since 4Q08

- Capital position strong
  - Continued to comply with all regulatory capital requirements
  - Continued to further strengthen retained earnings, which is a buffer against earnings volatility & potential future shrinkage
  - Due to retained earnings growth and strong capital position, lowered members’ minimum capital stock investment requirements in 2011 & 2012

- Dividends stable
  - Continued to pay stock dividends and repurchase excess stock
  - Recent dividends = upper end of fed funds target plus 12.5 bps
Housing finance: How does the competitive landscape shake out?

• GSE reform: future of Fannie Mae and Freddie Mac
• Qualified Mortgage (QM) – Ability to Repay rules
• Qualified Residential Mortgage (QRM) – Risk Retention rules
• Mortgage loan risk weightings
• Mortgage servicing rights capital treatment
• Housing price recovery

Regulatory reform: small bank vs. large bank impact

• Basel III capital guidelines
  — Leverage
  — Tier I
  — Buffers
  — Risk Weights
  — Mortgage Servicing Rights
• Basel III liquidity guidelines
  — Treatment of FHLB advances / other wholesale funds
• CFPB rules
• Dodd-Frank trickle-down effects
GSE Reform

Corker-Warner Draft Legislation

• 8 co-sponsors led by Sens. Bob Corker (R-TN) and Mark Warner (D-VA)
• The bill calls for liquidating Fannie and Freddie and replacing them with a single, government-backed entity – the Federal Mortgage Insurance Corporation – to explicitly guarantee mortgages
• The FMIC will be charged with helping to provide liquidity, transparency and access to mortgage credit by supporting the secondary mortgage market and production of residential MBS, as well as ensuring that all geographic areas have access to mortgage credit
• New public guarantor must be operational within five years of the bill’s enactment, at which point Fannie and Freddie will be wound down
• Fannie and Freddie’s affordable housing mandates would be repealed
• Public guarantor would serve as the FHLBanks new regulator, serving as a replacement for the FHFA
• The FHLBanks’ may apply to be issuers of covered securities, but must be approved by the FMIC to do so

FHLB of Dallas: Looking Forward

• Financially strong / prepared to grow

• Wide range of factors will affect the future
  – Economic conditions, excess liquidity, and member loan demand
  – Member regulatory changes
  – Basel III capital / liquidity rules
  – Housing finance reform / market changes
  – GSE reform / changes in future role
  – Changes in membership / industry structure