S&P Global
Ratings

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Federal Home Loan Banks

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Table Of Contents

Major Rating Factors

Outlook

Rationale

GRE Analysis: Critical Public Policy Role And Integral Link To The Government

Profile And Ownership: A Cooperative Owned By Its Member Institutions

Related Criteria

Federal Home Loan Banks

Major Rating Factors

None

Strengths:

- Government-related entity (GRE) with an almost certain likelihood of extraordinary government support
- Important to the implementation of U.S. government housing policy
- Important funding source for the U.S. banking system
- Very strong risk-adjusted capitalization
- Very strong loan asset quality and superlien position vis-à-vis depository institutions that has historically prevented losses on advances

Weaknesses:

- Concentrated exposure to the U.S. mortgage market
- Uncertain impact of potential legislative changes, though these are unlikely at least over the next two years
- Earnings decline when advance demand and interest rates are low, though profitability is not a priority

Outlook

S&P Global Ratings' outlook on the Federal Home Loan Bank (FHLB) System debt ratings is stable, in line with the stable outlook on the U.S. sovereign credit rating. We expect the likelihood of extraordinary government support for the FHLB System, if needed, to remain almost certain for at least the next two years. If we changed our rating or outlook on the U.S., we would reflect that change in our ratings and outlook on the FHLB System's debt.

In the long term, the FHLB System faces uncertainty related to potential legislative changes associated with the broader reform of U.S. housing finance policies. If initiatives were to gain momentum and target substantial changes to the FHLB System, such that the role of the FHLB System in housing finance and as a liquidity provider for the U.S. banking system were diminished, we could lower our ratings on the system's debt. To date, however, such initiatives have neither succeeded in gathering substantial political momentum nor targeted the FHLB System.

Rationale

The ratings on the senior debt of the FHLB System reflect S&P Global Ratings' view of the almost certain likelihood that the system would receive extraordinary support from the U.S. government if needed. We base this view on the system's integral link with the government and critical roles in promoting homeownership and providing funding to U.S. banks. Our ratings on the system's debt are at the same level as the U.S. sovereign ratings, even though the U.S. government does not explicitly guarantee the FHLB System's debt.

We view the FHLB System as one of the most important U.S. GREs. Promoting homeownership is a central and long-standing aspect of U.S. policy, which we do not expect will change. We believe the FHLB System has a critical public policy role in U.S. housing finance as a national liquidity provider to U.S. mortgage lenders, particularly during stressful conditions when private-sector liquidity is often unreliable.

Given its special public status as a U.S. government-sponsored enterprise (GSE), the FHLB System enjoys unusual advantages conveyed by the related legal framework. These advantages include lien priority over other creditors (without perfected and priority liens) in the event an insured depository member to which the system had loans outstanding fails. We also believe the Federal Housing Finance Agency (FHFA), the FHLBs' regulator, has clear and robust processes and procedures that enable effective governance, monitoring, and control of the FHLB System. These include administrative capacity and mechanisms for timely responses to any financial distress the system might encounter.

We continue to monitor legislative proposals and judicial decisions that could affect the FHLBs. That said, we do not anticipate any meaningful reform over the next 12-24 months.

In June 2021, the U.S. Supreme Court ruled the president can replace at will the director of the FHFA, effectively giving the president influence over the regulatory and enforcement priorities of the agency. Following the ruling, Mark Calabria resigned as director, and President Joe Biden appointed Sandra Thompson as acting director of the FHFA. Separately, in May, Senator Catherine Cortez Masto (D-Nev.) introduced the Federal Home Loan Banks' Mission Implementation Act. The proposed bill includes an increase in the annual set-aside for Affordable Housing Program obligations to 30% of net income, from 10% currently. If passed, this bill could lead to earnings pressure for the FHLBs because of the increased expense related to these programs.

The FHLB System has a diverse and global investor base, and it readily sells its debt at a small spread to U.S. Treasury obligations. In our opinion, the FHLBs' exceptionally favorable funding advantages are likely to continue as long as their policy role remains critical, and their link integral, to the U.S. government. Moreover, based on the history of ample funding for the FHLB System during periods of market stress in early 2020 and 2008, we believe access to funding is unlikely to be problematic even in stress scenarios.

The system has increased its reliance on short-term funding in response to member demands. However, given the generally match-funded approach to issuance, as well as the overcollateralization of advances to members, we believe the tenor of the system's funding remains manageable. The FHLBs' principal investments are GSE mortgage-backed securities, federal funds sold, interest-bearing deposits, reverse repurchase agreements, and municipal and Treasury securities.

The FHLB System consists of the 11 FHLBs. We assign stand-alone credit profiles (SACPs) to each of the FHLBs but not to the system as a whole. Because the system issues consolidated debt obligations on behalf of its component FHLBs, and in light of their joint and several liability for these obligations, we have issue ratings on the system's debt.

While we expect earnings pressure over the next few years due to excess bank liquidity lowering demand for advances, we do not anticipate consolidation in the system over the next 12-24 months. In 2015, FHLB Seattle merged with FHLB Des Moines--the only consolidation of the FHLB System in its 80-plus-year history.

The issuer credit ratings on the FHLBs are one notch higher than their 'aa' SACPs because, in our view, the likelihood of the government providing extraordinary support to them, if needed, is very high.

We view the FHLBs' business positions as strong, reflecting their established market positions in their districts, recurring business volumes, and public policy role, which we believe offset some of the risks associated with their lack of business diversity.

We view the FHLBs' capitalization as very strong based on their member-capitalized co-op structure and low-risk collateralized lending business. As of March 31, 2021, the regulatory capital-to-assets ratio at each of the banks comfortably exceeded the FHFA 4.00% minimum requirement. Capital ratios have risen as advances have decreased, resulting in reduced leverage. Because the bulk of the FHLBs' assets are advances to members, which have a relatively low risk weight in our methodology because all of the exposure is to financial institutions, we view their capital, on a risk-adjusted basis, as stronger than it might otherwise appear. As a result, we expect their S&P Global Ratings risk-adjusted capital ratios, based on our measure, to remain higher than 15% over at least the next two years.

Another factor supporting our ratings is that none of the FHLBs has ever suffered a loss on a collateralized advance to a member (reflecting both the lien priority and substantial collateral held against advances). Although we believe some of the collateral could be under strain because of the current economic headwinds, we believe the amount of collateral, at $2.3 trillion--or more than four times outstanding advances--as of March 31, 2021, offsets the potential for higher losses.

GRE Analysis: Critical Public Policy Role And Integral Link To The Government

We view the FHLB System as one of the most important U.S. GREs. In our opinion, promoting homeownership is a central and long-standing U.S. policy, evidenced by the tax deductibility of mortgage interest and the various activities of the U.S. Department of Housing and Urban Development. Such policy has, arguably, contributed to past U.S. housing market excesses. However, we do not expect this essential policy orientation to substantially change, given its widespread political appeal and the importance of consumption to U.S. economic growth (and homeownership to consumption, through wealth effects).

We think the FHLB System's critical public policy role to U.S. housing finance was clear in the U.S. mortgage crisis of 2008, during which advances (loans to client owner members) outstanding peaked at $1 trillion. The COVID-19 pandemic further illustrated the FHLB System's underlying importance to the U.S. banking sector in times of uncertainty and economic dislocation. During first-quarter 2020, advances swelled to $806.9 billion, a 25.8% increase sequentially, as member companies shored up liquidity to manage the stress. This marked the highest peak since the 2008 financial crisis.

In the following quarters, actions by the Federal Reserve and the CARES Act fostered substantial liquidity in financial markets and led to a significant increase in low-cost deposits at member banks. Consequently, advances fell at all FHLBs throughout the remainder of 2020 and continued lower this year. Net interest income contracted with falling demand for advances, in a trend we expect will likely continue into 2022 as elevated liquidity persists. FHLB advances ended the first quarter of 2021 at $399.1 billion, down about 50% year over year. The decrease in advances was more noticeable for commercial bank members than insurance companies. Commercial banks contracted to 39.7% of total advances from 63.3% year over year, while insurance companies (excluding captive insurance companies) grew to 30.6% from 16.2% for the same period.

Although the government does not guarantee the FHLB System's obligations, the system's status as a U.S. GSE provides several advantages. FHLB securities are eligible to be used for collateral that the U.S. Federal Reserve banks are required to hold against currency they put into circulation. The FHLB System is also exempt from almost all corporate taxation, and the securities it issues are exempt from state and local income tax. The U.S. legal framework also gives the FHLB System lien priority over other creditors (including depositors) in the event of the failure of an insured depository member with outstanding loans. Reinforcing these links to the government, the FHFA oversees all strategic decisions the system makes, and it closely monitors the system's financial condition.

We view the GSE Credit Facility (GSECF), temporarily established by the U.S. Treasury Department in 2008, as a clear indicator of the government's willingness and ability to provide extraordinary support to the FHLB System in times of stress. The GSECF proactively offered government loan liquidity to the FHLB System (along with Fannie Mae and Freddie Mac), if needed, asking for just the system's own advances as collateral.

Despite the absence of a government guarantee, we believe a close association between the system and the government is well entrenched in the minds of investors and other financial market participants. Together with a substantial amount of system securities outstanding ($697 billion as of March 31, 2021), we believe this association could mean that substantial financial distress for the system could harm the U.S. government's reputation, increasing the government's incentive to support its GSEs. Supporting this belief, FHLB consolidated obligations continue to price at a narrow spread over U.S. Treasuries, affording the FHLBs and their member institutions low funding costs despite the substantial volume outstanding.

In our rating analysis, we differentiate between the aggregate FHLB System and the individual FHLBs. The individual FHLBs' role is very important, and their link to the government is very strong. Because the 11 FHLBs have joint and several liability for the senior unsecured debt obligations that the FHLB's Office of Finance issues, we believe weakness in a single FHLB could affect investors' perception of the strength of the FHLB System as a whole. On the other hand, we believe each FHLB is less important, from a policy perspective, than the FHLB System as a whole. This is reflected in our assessment of both the role and the link of each individual FHLB as one degree weaker than our assessment for the system as a whole.

Because profit maximization is not a priority and each district has somewhat unique needs, we do not anticipate consolidation in the system over the next 12-24 months.

Profile And Ownership: A Cooperative Owned By Its Member Institutions

Each FHLB is owned by its member financial institutions. The member institutions are primarily commercial and savings banks, though they have expanded to include credit unions, insurance companies, and community development financial institutions (CDFIs). The membership mix as of March 31, 2021, was 64.2% commercial banks, 16.3% credit unions, 12.1% savings institutions, 6.5% insurance companies, and 0.9% CDFIs.

A member institution must purchase capital to belong to an FHLB. The member institution's stock requirement is generally based on its use of FHLB products, subject to a minimum requirement. In return, the member institution may borrow on a secured basis at typically attractive rates from its FHLB. Member institutions may also receive dividends on their shares in the FHLB, which helps lower their total transaction funding costs. Additionally, the system provides support for affordable housing and community investment programs.

FHLBs provide members with a reliable source of funding for housing finance, community lending, and asset-liability management, as well as liquidity for members' short-term needs. This funding is in the form of long-term and short-term secured loans called "advances." These advances are primarily collateralized by residential mortgage loans and commercial real estate loans, as well as government and agency securities. Community financial institutions may also pledge small-business, small-farm, small-agribusiness, and community development loans as collateral for advances. The FHLB System's combined advances totaled $339.1 billion as of March 31, 2021.

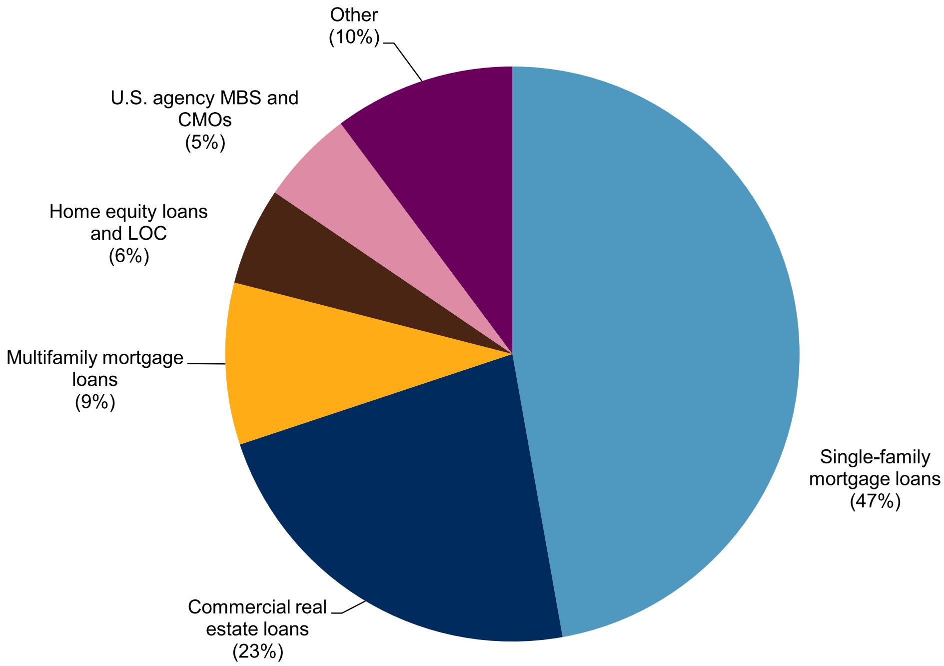
In addition to advances, FHLBs extend letters of credit to members--totaling $159.1 billion as of March 31, 2021. Members typically use letters of credit to secure public unit deposits, and the letters of credit would be converted to an advance in the rare event of a draw.

Although privately owned, the system is run as a cooperative for its member-owners. The system places more emphasis on retaining the capacity to quickly increase liquidity provisions, when needed, than on maximizing current profits. We believe the FHFA's close oversight reinforces this strategy.

The FHLBs have recently been moving toward floating-rate bonds, replacing discount notes, in response to market demand and to address the FHFA's concerns regarding maturity gaps, though in many cases the bonds are short term. Short-term funding (with a remaining maturity of less than one year) made up 70% of consolidated obligations as of March 31, 2021. Total consolidated obligations were $696.9 billion in book value as of March 31, 2021. We believe the system's transition from LIBOR-based funding toward funding based on the secured overnight financing rate could be smoother than for other issuers, given this larger percentage of short-term debt.

Chart 1

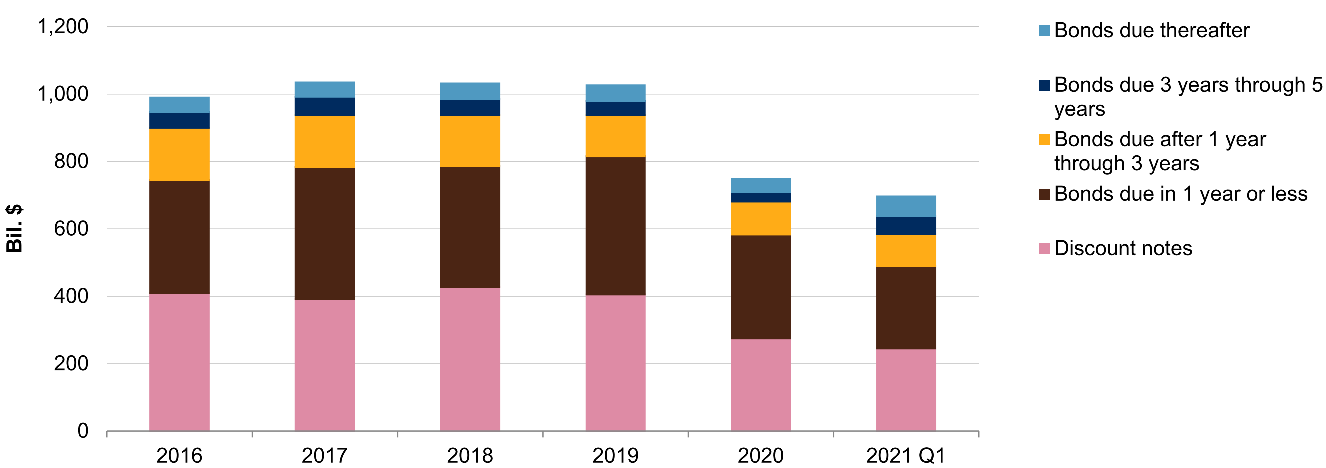
FHLB Percentage Of Collateral Securing Advances
As of March 31, 2021



Source: S&P Global Ratings.

Chart 2

FHLB Consolidated Obligations By Contractual Maturity

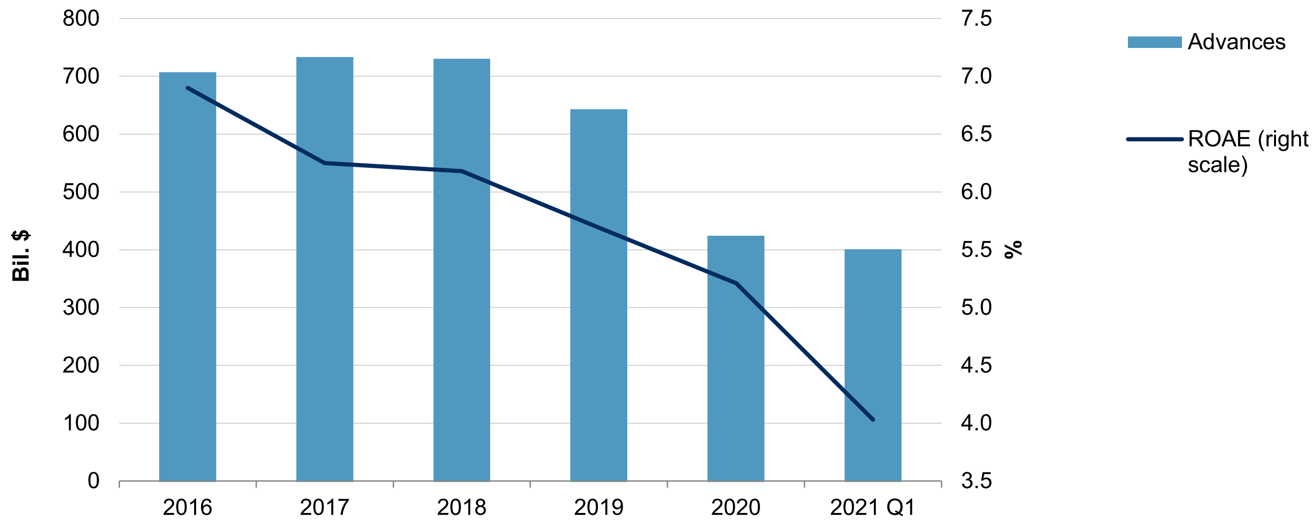


Source: S&P Global Ratings.

Chart 3

FHLB Advances And Profitability

Advances have declined meaningfully as a result of COVID-19



Source: S&P Global Ratings.

Related Criteria

- Criteria | Governments | Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | General: Issue Credit Rating Methodology For Nonbank Financial Institutions And Nonbank Financial Services Companies, Dec. 9, 2014
- Criteria | Financial Institutions | General: Nonbank Financial Institutions Rating Methodology, Dec. 9, 2014
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- ARCHIVE | General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Ratings Detail (As Of August 5, 2021)*	
Federal Home Loan Banks	
Senior Unsecured	AA+
Senior Unsecured	AA+/A-1+
Senior Unsecured	AA+/Stable
Short-Term Debt	A-1+
Short-Term Debt	AA+/Stable
Sovereign Rating	
United States	AA+/Stable/A-1+
Related Entities	
Federal Home Loan Bank of Atlanta	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Boston	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Chicago	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Cincinnati	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Dallas	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Des Moines	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Indianapolis	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of New York	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Pittsburgh	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of San Francisco	
Issuer Credit Rating	AA+/Stable/A-1+
Federal Home Loan Bank of Topeka	
Issuer Credit Rating	AA+/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.