Advancing Forward
Annual Meeting Webinar, May 14, 2020

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Introduction

Andrew S. Howell, President & CEO

Good morning and welcome to the Federal Home Loan Bank of Cincinnati annual stockholder meeting, and the first such meeting to be held by webinar. Judging by a few of the comments I got on the Q&A, folks out there can see the slide that is up on our welcome slide here.

Obviously, we're truly operating in an unprecedented time and we thank you for taking some valuable time out of your day to spend with us today. We will share comments from the board level, provide a review of 2019 and the first quarter of 2020 performance of the Bank and review updates on district demographics and Bank programs.

We will discuss the impact of the current environment on the economy, industry members, and the Federal Home Loan Bank as we all try to move forward in a positive but realistic manner as a bit of a preface to this session.

I want to make sure you understand the Federal Home Loan Bank is fully functioning through the combination of a very unlimited onsite physical workforce of about five to ten percent of our staff, which is about 15 folks collectively from our main office in our backup facility in a northern Cincinnati suburb with the remainder working remotely from home, and just like you, our primary approaches to keep our staff safe and best positioned to provide full-service access to you, our members.

While we have all had to make changes to the way we conduct our daily operations, my hope and expectation is that you have not experienced any meaningful interruption in access to Bank products or services. In our comments today, we'll discuss some of the operational changes that have taken place, new and expanded assistance programs, and what may be on the horizon.

In that regard and keeping with appropriate social distancing the presenters for today's session originating from three separate locations.

So, a technical miracle here in some sorts and we'll include the usual line up of our Chairman, Don Mullineaux, yours truly here from Cincinnati and Kyle Lawler, our Executive Vice President, Chief Business Officer remotely as well. We did not include an outside economist for this session as we normally do a given the extreme uncertainty of the environment, but we'll touch on a few economic and industry factors.

Before we get started with the formal comments, I will note that everyone is muted upon arrival to the webinar and will remain muted for the duration of the webinar. You have the ability to submit questions throughout the presentation by addressing them to the Q&A box for the host and presenter, and instructions are provided on this particular slide. We will respond to questions at the end of the presentations, or follow up individually if any of the questions are members specific.

We've got ninety minutes scheduled for the webinar and expect the presentation to be sixty plus minutes. There should be plenty of time for covering questions at the end but we can go a little bit longer if we need to.

Forward-looking statements

Our presentation materials have been furnished to the SEC in a Form 8-K and are available on our website under Financial Results. Please note that today's discussion may include forward-looking statements, based on our view of market conditions and our business as we see it today. These elements can change due to changes in our business environment or in market conditions.

Talking about forward looking statements and being cautiously optimistic about the future, we do hope to see you in person at one of our member appreciation outings that we are targeting for late summer, early fall at the same venues originally intended for the regional meetings. We'll have to wait and see how things play out in terms of that but that's our plan right now, and we will keep you informed of those events and schedules in the coming months.

So, with that, I would like to introduce our first official speaker today and that is our chairman, Dr. Don Mullineaux, to kick off the formal presentation. So, Don, I'll turn it over to you.

Chairman’s comments

Donald J. Mullineaux, Chair of the Board of Directors:

Thank you, Andy and good morning everyone. I also want to welcome all the members, directors, trade association leaders, Affordable Housing Advisory Council members and Bank staff who have logged into the meeting. I hope that you, your families and loved ones, employees and colleagues all remains safe and well in these extraordinary and trying times.

Let's begin as we typically do with a review of the Board’s recent activities.

Last November, we ratified the results of the 2019 director elections. In Ohio, members re-elected Bob Lameier, President & CEO of Miami Savings Bank, to a new four-year term. Jonathan Welty, President of the Ohio Capital Finance Corporation in Columbus, was elected to his first term. And the Board appointed Kathleen Rogers, Executive Vice President of US Bank in Cincinnati, to fill the remainder of the term of a director who had resigned from the Board.

Two Independent directors were re-elected: Charles Ruma, President of Davison Phillips Inc. in Columbus and yours truly, who hails from Lexington, Ky., I'm grateful for your continued support.

Internally the Board reelected Jim England to a two-year term as Vice Chairman.

Sadly, we must bid a fond farewell to Mike Melvin, President and Director, Perpetual Federal Bank, Urbana, Ohio, who served as a director for 21 years. We miss Mike's counsel and his wry wit, I can assure all of you.

The 2020 director elections will soon be underway and will be conducted for the first time electronically. Subject to the approval of our regulator, we expect members will be voting for two open Member seats in Ohio and three Independent director seats. In Ohio both Member directors are eligible and they are Brady Burt, CFO of Park National Bank in Newark, and Jim Vance, Senior Vice President and Treasurer of the Western and Southern Financial Group in Cincinnati.

Only one of the Independent director seats can be sought by an incumbent. And that is the current Chair of our Audit Committee, Lynn Anderson, a retired banking and insurance executive from Columbus. The Board regrets it will lose the valuable services of Leslie Dunn, a retired partner of Jones Day in Cleveland, and Alvin Nance, the CEO of LHP Development & Management in Knoxville, since each of them is term limited.

Andy Howell will speak extensively to the Bank’s financial performance, but let me briefly touch on some current and regulatory issues, as well as our efforts to fulfill the Bank’s housing and community investment mission. As you may know, the issue of membership in the Federal Home Loan Bank System has resurfaced in our nation's capital. Our regulator has issued a Request For Information about the factors to be considered about who should be eligible to join the Federal Home Loan Bank System.

The Federal Home Loan Banks have responded as a collective, and each bank has shared the letter with both their national and state trade associations. The comment period is open until June 23 should you likewise wish to respond. Our staff would be happy to respond to any questions you have on this issue.

Locally and in Washington, your Home Loan Bank engages on an ongoing basis with committees that have jurisdiction over us. In Ohio, this includes Representatives Steve Stivers, Joyce Beatty, Anthony Gonzalez and Warren Davidson. In Kentucky, Andy Barr, and in Tennessee John Rose and David Kustoff. In the Senate, we consult with ranking member, Sherrod Brown of Ohio. With your help, we generally find an open door to expressing our views on issues that may affect all of our members.

The Board is continuously committed to satisfying our housing and community investment mission. In addition to the affordable housing allotments, the Board renewed the Bank's voluntary support programs in 2019 and 2020. To date we have distributed more than $3.9 million to the Disaster Reconstruction Program to help 275 households rebuild after natural disasters in the three-state district. Through the Carol M. Peterson fund, the Board approved $2.1 million in 2019 to help 303 elderly or special needs households with emergency repairs.

Last year Directors, Senior Management, Advisory Council members and Bank staff worked with over 1,500 volunteers to build 21 homes as part of the Jimmy and Roslyn Carter Work Project in Nashville. The Board also approved a new Advance program and modified its existing discounted Advances to directly support the COVID-19 related lending activities of our members, and you will hear much more about these initiatives from Andy and Kyle.

Please know that the Home Loan Bank is here for you. We remain open for business in whatever form it takes to meet your needs. We appreciate your support and patience, and your partnership.

Now as Andy mentioned, we typically have invited economists to our shareholder meetings. We did not want to give short shrift to the unprecedented developments in our economy. So I'm going to put on my professorial economist hat and spend just a few minutes with you on what might lie ahead.

We're going to look at only two charts and each conveys a picture like nothing I have ever seen since receiving my Ph.D., now 50 years ago.

The first is the unemployment rate for April, which has surged from a five-decade low in February to 14.7%. To the surprise of many, the stock market initially took this as good news since investors were expecting an even higher figure. But the Bureau of Labor Statistics told us in its announcement that the number was probably understated by roughly five percentage points.

Treasury Secretary Mnuchin believes we are headed to at least 25%, and this week the economists at Goldman Sachs agreed with him. Some private forecasters believes at peak will reach an all-time high of

30%. If you need another startling statistic, the number of jobs lost in March and April exceeded the number of net jobs gained over the last 10 years.

As you know, the government releases data on real GDP on a quarterly basis. The first quarter number showed a decline a 4.8%.

The second chart we're seeing is the Weekly Economic Index produced by the Federal Reserve Bank of New York, and it is based on 10 economic indicators that are available either on a daily or a weekly basis.

The way to interpret the number is that if the index maintains its value through the rest of the quarter, GDP would be 11% lower than it was a year ago. We're only at the midpoint of the second quarter, but the index indicates that in less than two months, this contraction is already worse than the Great Recession. Economists are projecting declines in GDP for the second quarter that range from 25% to 40% at an annual rate.

If you want to be your own economist, I suggest you follow this index on the New York Fed website. Once you see it turning upwards for several consecutive weeks, it's a strong signal the economy has found a bottom. But since I sent this chart to the Home Loan Bank for use in our presentation, the index has dropped another percentage point.

I'm sure you've seen speculation about the nature and shape of the economic recovery. While as many as half of the forecasting community was initially anticipating a V-shaped recovery that would begin in June, that optimism has waned, and many forecasts now envision a hockey stick, or as some call it a Nike swoosh-like pattern to the rebound.

Most economists believe the unemployment rate will not drop below 10% until sometime next year. Since the outlook depends on our progress combating the virus, and on the likelihood of more government actions to shore up the economy, as Fed Chairman Powell has indicated, there has never been so much uncertainty about the future path of the economy.

To fund the sizable economic support programs in place and some yet perhaps to come, the Treasury will issue between $5 trillion and $6 trillion in new debt this year, more than three times the previous yearly record for government borrowing. The Fed's extensive liquidity and credit facilities have ballooned its balance sheet to almost $7 trillion, and at least one forecast places it above $10 trillion by year-end. The Fed will probably purchase on the order of two-thirds of all new Treasury debt, as well as buy for the first time as much as $750 billion in corporate bonds.

Despite the massive increase in public and private debt, short-term interest rates are likely to remain near zero well into next year, and long-term rates are not expected to exceed 1% over that same horizon. In fact, a few analysts believe the 10- year Treasury rate will drop below zero for as much as several quarters.

Whatever the shape of the recovery, surveys show that about 8 in 10 furloughed workers expects eventually to return to their old jobs. But researchers at the University of Chicago have built a model predicting the actual outcome for retained jobs is more likely to be 42%. If they are correct, the catastrophic condition of the labor market will linger for quite some time and economic policy needs to be shifted towards supporting the creation of new jobs to replace those that will be permanently lost.

If you are tempted to think that the pandemic is a black swan-like event that could never have been anticipated, I recommend that you read the article called "The Warnings" by David Quammen in the May 11 issue of *The New Yorker* magazine. It shows there were multiple missed signals over the last two decades that suggests the crisis we face represents, to a significant degree, a failure in risk management at various levels of government.

Believe it or not, not all the news you're going to hear this morning is bad. I'm going to turn the program over to Andy Howell, who will take a brief look back at our reasonably solid performance in 2019, but spend most of his time talking about the challenges that lie ahead.

Thanks once again for joining us this morning.

CEO's comments

Andrew Howell:

Thank you, Don. That's a tough act to follow here in terms of that particular news. But, thanks again, to you, and thank you, to our Board of Directors, as Don mentioned, who have remained actively engaged, supportive of the Bank's strategic direction, and certainly responsive to the changing needs of our Fifth District members.

I also want to recognize Mike Melvin for his many years of valued service on the Board. His guidance and counsel over the years was greatly appreciated by all of those who came in touch with him, including myself.

Our theme as you see today for the annual report and the 2020 stockholder meetings is Advancing Forward, which was developed originally in the context of strategic initiatives aimed at strengthening our core banking operations to better serve our members as we move into the decade of the '20's.

It's about how we look to the horizon and beyond, and how we will position the Bank to be a trusted and reliable partner for many years to come. Our compass is our mission, our vision and our values. In 2019, we applied these to a stronger and more deliberate strategic planning process, aimed at making our operations more efficient and ready for future opportunities, challenges and creating more value for your membership. And we are certainly starting 2020 off with some mighty challenges here.

The agenda for our presentation today will look back as Don said at the past few years for both the industry and the Federal Home Loan Bank to set the stage for where we are today. Although I will focus a bit on 2019 performance, that has become more of a distant memory as we turned to the first quarter of 2020, the rapidly changing environment, the COVID-19 impact on all of us and an eye on the future, which may be more immediate, rather than long term until we see how things play out as the economy tries to reopen. But I think we can all agree that the outlook for the future has changed dramatically since the beginning of March.

Member performance

The general state of the banking industry and Fifth District members is strong, and that's good in this particular environment, obviously. Over the past 10 years the industry steadily strengthened balance sheets through loan quality, capital growth and consistently stable returns.

2019 started out the year with the expectation of rising interest rates, given at least, at the time, a robust economy, low unemployment, and generally favorable outlook. From about May of 2019, interest rates started a downward trend due largely to an escalated US-China trade war and a slowing economy of sorts. Lower rates led to narrowing net interest spreads, but still strong performance on excellent asset quality and related provisions. So, overall, 2019 was still a good year for member performance.

However, as you see here, that was quickly and meaningfully impacted in the first quarter of 2020, that was evidenced by the nearly doubling of the loan loss provisions, which impacted returns and ultimately capital ratios through rapid loan growth. I suspect that most of this happened during the last few weeks of the quarter. I will cover how some of these changes impact other aspects of the industry and our business activities in just a minute.

Loans and deposits

We always like to review the industry loan-to-deposit ratio since it's a key driver of activity by the large majority of our member base and, in turn, what borrowing needs from the Federal Home Loan Bank may be. Clearly deposit growth has continued to outpace loan growth in recent years, moving that ratio from 77% in 2018 down to 73% near the end of April, based on the weekly Federal Reserve reporting. So, this explains the declining use of Advance balances in recent years, given fairly flat loan growth, the abundance of low-cost deposits, and certainly stagnant-to-falling interest rates throughout the latter part of 2019.

But that all changed in late March, due to the pandemic, as loans moved up quickly in a brief period of time, followed by a significant jump in FHLB Advance usage, and ultimately a very large jump into deposits as funds from the various federal government stimulus legislation starts to go directly into the taxpayer bank accounts. And normal federal tax payment outflows from member deposits were pushed back as well, so even more of an abundance of deposits by late April.

Financial institution loan loss reserves

I noted the first quarter increase in loan loss reserves for our district specifically, a few slides earlier, but this is a more dramatic look at the quick impact on provision of commercial banks, specifically, in anticipation of losses. This is more than a 25% jump in reserves in a little over one month. Let's hope losses don't get that extreme, but certainly time to start thinking and planning for what might be a hit.

FHLB Cincinnati: Mission-related activity and investments

Now, let's take a look at the performance of your Federal Home Loan Bank, over the same time frame: a fairly stable-to-reducing balance sheet, as the reduction in member Advances demand is steady for the reasons noted earlier from 2016 through 2019. During that time Advances reduction was offset by increased investments and steady growth in the MPP, but still a net reduction in overall assets of about $10 billion. Some of that reduction was offset by a sizable increase in lower yielding liquidity investments as our regulatory liquidity requirements were increasing, starting in early 2019 all throughout the year.

During that period our Primary Mission Asset Ratio remained above the regulatory preferred minimum of 70%, and that ratio is of our core mission assets, primarily Advances and MPP, to total debt issued, which we refer to as consolidated obligations. But as I said earlier, things can turn quickly, and as a wholesale bank, we and the Federal Home Loan Bank System were prepared to serve as a first responder when the pandemic hit. And we certainly did just that by more than doubling our Advance balances in less than a month, as we were about the $35 billion dollar-level in Advances in early March and ended the month as you see here at $80 billion.

FHLB Cincinnati: net income

Okay, let's shift gears and take a look at the earnings performance of the Bank. As you can see, we peaked with record earnings in 2018 as interest rates were steadily increasing and Advances were in the $50-to-$60 billion range. Both of those factors started to decline throughout 2019 and into 2020 even without the pandemic impact. The first quarter earnings of $80 million is certainly coming out of the gate strong, but heavily influenced by the more recent events and included higher non-interest income primarily due gains on the sale of certain derivatives during the first quarter. Although net income was higher in the first quarter, net interest income was down due to higher net amortization on mortgages and prepayments driven by the lower rates that were mentioned earlier.

Similar to the rest of the industry, those falling interest rates led to shrinking net interest margins in general and creates challenges managing a fixed rate mortgage portfolio through refinancing, repayments and again accelerated premium amortization. So you have increased expense impact now on the early repayments and new loans going the books at lower yields and spreads. In addition, we have increased amounts of lower yielding liquidity investments. This trend was expected to continue into

2020 and combined with the uncertainty of the pandemic impacts were obviously driving factors in the decision to reduce the dividends when it was declared in mid-March.

FHLB Cincinnati: capital growth

From a capital growth perspective, the capital base is a source of strength for the Federal Home Loan Bank System. Capital is made up of a combination of member owned stock and retained earnings. As a little refresher, both of those categories have multiple components, but in total must exceed the regulatory minimum of 4% with a little bit of a management cushion added in there, but not too much, or it creates a drag on the dividend rate payable. We typically maintain a 4.5%-plus ratio and have tended to conduct global excess stock repurchases when that level rises above 5% in addition to the other variable factors.

As you may be aware, all members have stock purchase requirements based on membership as a percentage of assets subject to a $30 million cap per member. The 2020 annual update process is actually concluding today, so please return your form today if you haven't already done so, or you can expect a call from one of our staff to complete the process.

In addition, every member has an activity stock requirement based on the level of borrowings or MPP loans sold to the Home Loan Bank. This amount will vary by the activity level of the member and the amount of cooperative excess stock available. That part of the Capital Plan came into play more prominently for some members during the historic jump in Advance usage in March, and has led to some adjustments to the plan that I will address in just a few minutes.

The second component of capital is retained earnings. Every Home Loan Bank is required to set aside 20% of net income in a restricted retained earnings account until the restricted amount exceeds 1% of the Federal Home Loan Bank debt, or again, the consolidated obligations. Currently, for our Bank that level would be about $1 billion. The Bank's total retained earnings position of nearly $1.2 billion provides a cushion and lessens the risk of any future impairment of your Federal Home Loan Bank stock ownership. Just by way of note the Federal Home Loan Bank System started with basically zero in retained earnings in the year 2000.

Current Treasury yield curve

Now, let's take a look at the Treasury yield curve and the 10-year term more specifically. Don referenced this a little earlier. Obviously, a function of the economic environment and a material factor of our business activity and earnings. Since mid-2019 to the end of February 2020, the curve has been flat to inverted at various points along the curve. As I noted earlier, this has created a number of challenges in managing the balance sheet with respect to lending activity, related hedging strategies and derivative valuations. I'm not making any statement about what's causing the changes – whether it's trade wars, a slow economy, the pandemic – but the ultimate rate levels can lead to certain market actions that impact business activity and earnings.

On Tuesday of this week, a new 10-year Treasury issuance was auctioned at 70 basis points, I think in the amount of about $32 billion, which was apparently well received by investors with a bid-to-cover ratio of nearly 2.7 times, which was the best offering the past five years. As of today, that 10-year sits in the mid-60 basis point range. It's hard to think that the 10-year Treasury could drop much lower than the 50 basis point historic lows that were reached in early March. With talk of the potential for negative rates, as Don mentioned, certainly nothing is off the table at this point.

Mortgage originations

One of those impacts from lower Treasury yields is a shift in the mortgage market from a purchase to refi market that started in mid-2019 and accelerated in early 2020. Right now, the 2020 level of refinancing is projected much higher, but could be slowed somewhat by pandemic impact. The origination pipeline is slowed by the high volume of borrowers seeking forbearance on current loans and job losses impacting credit eligibility of borrowers looking to refinance. In addition mortgage rates in general are not falling as low as they might normally do in an economic environment such as this.

A rapidly changing environment

So as Don covered a couple of these points earlier, obviously, until you see what's transpired in April, you see the full impact. Unemployment went to that 14.7% in two months and as he says estimated to be as much as 20% which is depression era levels and likely higher.

As a result, certainly the mortgage forbearance rate has skyrocketed from 25 basis points to 7.5% as we've seen over the course of the past couple of months. In two unscheduled meetings in March, the Federal Reserve quickly reacted by lowering the effective funds rate or the target Fed Funds rate by 150 basis points to the zero-to-25 basis point range. Currently that's trading in the five basis point range. So, we're getting very close to zero or negative rates.

Housing market upheaval

One of the results – and this is something we've seen in recent years – is the biggest housing upheaval since the financial crisis. Existing and new home sales dropped quickly and the understandable reduction in housing starts will certainly create an even deeper hole of available housing inventory to meet the growing demands of homeownership that was already having challenges digging out the last housing crisis.

Federal Reserve balance sheet expansion

So, in addition to dropping the Fed Funds target rate, the Fed took rapid and substantial actions to stabilize the financial markets and keep credit flowing. Obviously, they used their emergency lending powers to establish a multitude of programs, targeted to a wide range of markets, industries and consumers.

The program most impactful to our members is the PPP facility, which provides the potential for grant funding to your business customers to support job retention and ongoing viability in the small business community. Between two congressional bills, there's been approximately $700 billion in PPP funding authorized. We'll talk more about how the Home Loan Banks have been able to help support our members that are actively using that particular program.

Very simply, the impact on the Fed balance sheet has been massive, adding $2.5 trillion in less than two months. As Don mentioned, it will most certainly move higher than the $6.7 trillion current level that it's at. As he said, some are estimating $10-$11 trillion in program funding before it's all done, which isn't unrealistic given the proposed House stimulus bill that came out yesterday and the comments by Federal Reserve Chairman Powell yesterday as well.

FHLB System Advances

From a Federal Home Loan Bank System standpoint, we think the system is uniquely positioned as a first responder to financial services industry liquidity needs and serve that mission well, through many challenging times, at least over the past 30-plus years that I've been part of the System. The wholesale structure of the System allows for the rapid expansion and contraction to quickly meet the liquidity needs of our members or to scale back when lower cost deposits are plentiful. The Cincinnati Bank ranged from $27 billion to $80 billion over the past 10 years. Obviously, we hit the $80 billion dollar mark just recently. The core level of Advances is more likely somewhere between $25 to 45 billion to meet the asset/liability management and long-term funding needs of a fairly diverse membership of depository institutions and insurance companies.

Capital stock utilization

Capital stock – let's take a minute to talk about that. The Federal Home Loan Bank System is self-capitalizing with minimum capital requirements, a component of which is provided by member activity stock. I mentioned earlier the membership stock component of that. This activity, currently Advances and MPP, has required capitalization of 4%. But when there's an abundance of excess stock, the Capital Plan – and that's the Cincinnati Capital Plan – provides for the reallocation of that access stock between members that can range from 0% to 4%. This cross capitalization aspect of the plan was designed in 2003 so that the aggregate amount of stock doesn't grow to levels that start to dilute the earnings ability of the Bank. For 17 years now the plan has worked extremely well with limited instances, maybe we can count one hand, the number of days where we had experienced the full utilization of the cooperative access stock pool.

That occurred most recently in March due to the significant increase in Advance usage. For those of you that were impacted, you know that even though you may have had individual excess, that stock, which you still own and receive a dividend on, was then being utilized by another member given your own level of inactivity up to that point. When the excess pool is turned off or fully utilized, all members have to buy stock at the maximum activity level for any new Advance or MPP sales until Advance levels decline and the cooperative excess stock pool is once again available.

Now, that situation would typically show up in your additional borrowing capacity report on the Members Only site, and it would show up with a zero availability of Advance capacity based only on your stock requirements.

It simply means that a stock purchase is required and could even be netted out of what is borrowed if that's desired. Now I want to make clear that this doesn't mean that the Federal Home Loan Bank was at any time in a compromised capital position. To the contrary, we were making the most efficient use of all the capital available. We do realize that the unusual structure of the Capital Plan may not be fully understood by all members and appreciate the challenges and understanding the nuances, especially in stress periods like we recently experienced. But keep in mind that as a wholesale entity, we can expand and contract our balance sheet quickly, which may at times require stock purchases to support member activity growth and other times involved stock repurchases so that we can most efficiently manage our capital position and dividend.

FHLB Cincinnati Capital Plan update

So, what does this mean going forward? Well, there's going to be some incremental changes in an effort to reduce the reliance on the cooperative excess stock component of the Capital Plan. That will result in changes to the activity stock requirements noted on this slide. The current activity stock requirements for Advances are a minimum of 2% and maximum of 4%, while the minimum and maximum for MPP activity is 0% and 4%. The difference between the minimum requirement and maximum requirement is either filled by cooperative excess stock if available, or by a member’s stock purchase at the time the activity is initiated, as I mentioned earlier. Excess stock is shifted within the Capital Plan to maintain the capitalization of all activity at the current maximum level of 4%.

In an effort to reduce the reliance on cooperative excess stock and support increased liquidity requirements, the Bank will be announcing a change in activity stock requirements that would be effective 30 days from the member notice. So that's likely to be in late June. The change will be an increase in the Advances minimum to 3% and a maximum of 4.5%, while the MPP change would be to a minimum of 2% and the maximum will remain at 4%. Again, these changes will be on a going-forward basis on incremental or new activity with an expected implementation date of late June. This will affect each member slightly different depending on the level and type of activity. In some cases existing excess that you have will simply be reclassified as activity stock with no additional purchase requirement. A formal notice will be sent to all members within the next few days announcing this change in the plan.

I also want to make you aware that the Bank does not currently require activity stock to support Letter of Credit activity, which is not consistent among all Federal Home Loan Banks. However, all Federal Home Loan Banks, including us, will implement such requirement by year-end 2020. We expect it to be a *de minimis* amount of 10-20 basis points on the notional amount of the Letter of Credit issuance, and that's compared to the 4.5% or 4% maximum amounts on the Advances or MPP. So, please keep an eye out for that particular NewsLine in the coming days and feel free to contact us with any questions regarding the specific impact on your stock requirements going forward.

FHLB Cincinnati: housing program changes

Another change driven by the current environment is our housing programs. Don had mentioned these briefly in his comments. In an effort to respond to the immediate impact of the pandemic and provide support to our members, the Board quickly approved the new RISE Program, which stands for Responsive, Inclusive, Supportive, and Empowering, and expanded the existing community investment and economic development programs. These programs allowed us to get very low-cost funding into the hands of our members, for terms of six months at a 0% rate, which allows for up to $5 million per member, and at least $2 billion in total availability. And up to $50 million per member is available under the CIP and EDP programs at the Federal Home Loan Bank's cost of funds for a total program limit of $1.5 billion. Eligibility access is very broad and easy to get, in scope to everything that is COVID-19 related, whether that's PPP loans that you have done, they don't have to be pledged to us as collateral but qualify as eligibility; loan forbearances; deferred premium payments for policy holders, anything along that line. So, very broad in scope in terms of eligibility. Please contact the Housing & Community Development Department to obtain eligibility approval and then complete the appropriate Advance application to access the funding.

Keep in mind, the funding is provided on first-come, first-served basis until funds are fully exhausted. Eligibility approval doesn't guarantee the funds' availability, so don't delay in drawing down the funds once you are approved, but you don't have to do that immediately. So, hopefully everybody can take advantage of that particular program change.

Strategic initiatives

On the strategic initiatives side of things, another way we're trying to move forward in enhancing those initiatives is our engagement with members in helping shape products, services and operational processes. In that respect, we have established a Member Advisory Panel, and that panel consists of 16 members, eight in Ohio, four in Kentucky and four in Tennessee. We've got bank, thrift, credit union and insurance company members represented, and the asset sizes of these entities range from $100 million to over $100 billion. I want say thank you to those that have agreed to participate.

We're in the process of obtaining more specific survey information on various topics from this group as we look to have the first meeting in the fall, rather than as planned in the summer originally. We look forward to the focused feedback from this group, and we'll rotate new members into the group over time.

In addition, the Bank established an internal operations SWOT team of sorts to look at ways of improving our member experience in dealing with the Bank. Much of this may involve technology applications, communications, and online transaction capability. While this group is currently interacting with members that are frequent or targeted users of specific products and services, the expectations is that the Member Advisory Panel will eventually serve in this role over the long term.

Electronic voting

As Don noted, in the spirit of trying to be more efficient and expand our use of technology solutions with members, we will be utilizing online voting for the 2020 director election, that Chairman Mullineaux referenced in his comments. We have sent out information regarding the process and it is also provided on the Members Only website. We do want to ensure that we have the appropriate contacts for each member. Please let us know if you'd prefer to vote the old fashioned way and we will accommodate that approach as well for this year.

System legislative recommendations

As many of you may have heard during our state trade group calls that we did about a month ago, the Federal Home Loan Banks were asked by various members of Congress what changes would be beneficial to help the Federal Home Loan Banks better support the economic recovery response to the pandemic.

It's always a double-edged sword. As we communicated to both Congress and our members, we asked for expanded collateral eligibility on government-guaranteed loans – and that was specifically SBA-related, which right now, that guarantee does not flow through to the Federal Home Loan Banks. And we were asking PPP loans as well, relative to that; that's a temporary fix so we can do that but not a legislative fix. We asked to expand the CFI – the community financial institution definition – from $1.1 billion to $10 billion, and that's consistent with the Federal Reserve definition, and that allows for some expanded collateral acceptance as well. Then we asked to codify and expand the ability to issue letters of credit; that's currently allowed under regulatory authority.

Now, with any congressional negotiations that go on there is the potential that any legislation could impose more assessments or taxes or expand programs or other requirements that may not be in the best interest of the Bank or our members.

If that happened, certainly, the Bank will argue against any such legislation. The recently proposed bill by the House did not incorporate any of the requests I just went through with you, but it also did not include any undesirable changes as well. We'll keep our members and the respective trade groups informed on the future developments and actions as necessary along that line.

Current and future developments

Keeping an eye out to the future here, taking a look down the road, I have a few things to share with you. The first, and Don covered this in his comments as well, is a Request For Information on membership that the Finance Agency put out earlier this year. That's in response to a 2019 Treasury Department report regarding Federal Home Loan Bank membership. The agency is evaluating the potential expansion of membership to entities such as mortgage bankers, mortgage servicers, REITs, FinTech companies, or any other such entity that has a nexus to the residential mortgage market.

While I don't think either – well I know the Federal Home Loan Banks don't, nor the Finance Agency, want to expand the System membership. Those segments certainly have strong lobbying groups and have been extremely active in pursuing that access.

In the past, the Agency has deferred to congressional authority in determining who should have access to the System. So, absent a legislative change, I really don't expect to see any expansion in membership eligibility. The Federal Home Loan Bank System did submit a joint comment letter on April 22. We shared that with all of our state trade organizations and outlined a number of aspects that the Federal Home Loan Banks would or would not like to see happen – and that would be, that it should not negatively impact eligible collateral; it shouldn't adversely impact existing members; new members should be subject to prudential regulation; new members should have a clear nexus to housing; and the Federal Home Loan Bank should retain the discretion to approve qualified applicants. The deadline for submitting a comment is June 23.

I also want to bring your attention to the rapidly approaching termination of the LIBOR index on December 31, 2021. The date is holding firm and is a sizable change for the industry and financial markets, and a substantial operational challenge given the volume of LIBOR-indexed transactions around the world.

The Federal Home Loan Banks are actively involved in establishing a reasonable replacement with the SOFR index and we are collectively the largest issuer of SOFR debt in the world. We've held several events with members and market participants to keep the transition process moving forward. Kyle will talk a little bit more about that in his presentation.

And lastly, as I said earlier, you're now aware that the PPP loans are eligible as Home Loan Bank collateral. We announced that on May 4th. Our ability to accept these loans took quite a bit of coordination and accommodation between the Federal Home Loan Banks, our regulator, the Finance Agency, the SBA, and the Federal Reserve. But, ultimately, we made that work. So, we've already started to see some members take the opportunity to pledge that particular collateral to borrow against. Again, Kyle will give a few more details on this during his comments.

Closing remarks

Okay, wrapping up here on my section, let me say that I appreciate the opportunity to serve our members and share the details behind how the Bank has performed over the past year, the impact of the current pandemic on the economy and our collective business and how we're all trying our best to move forward. Similar to you, our highest priorities are focused on the health and safety of our families and staff, which is very much an overlap for most of us. That also allows us to remain in the position of being reliable business partners for our members and helping meet the needs of those that depend on you. As always please reach out if there's anything we can do to improve upon that process.

So, with that, I will turn the presentation over to Kyle Lawler and respond to any questions, following his comments. Thank you.

CBO presentation

R. Kyle Lawler, EVP, Chief Business Officer:

Thank you, Andy, and first let me thank you, all of our members for taking time out of your busy schedules to spend this morning with us and to hear about the direction where your Home Loan Bank is headed.

Our presentation will follow a very similar theme that Andy and Dr. Mullineaux had introduced. My focus will be more specifically on the Cincinnati Home Loan Bank.

Membership composition and assets

We always typically put up a slide for the composition of our membership and how it's evolving over time. You can see that the number of charters in our district has been declining since 2010 through now. In the box on the right you can see the changes. Commercial banks, we've lost the largest number. Savings banks and thrifts, lost 46, and increase in credit unions, insurance companies and CDFIs, for a total loss of 101 charters out of our district. However, what this doesn't show, or what's masked in here, is that over the same time frame your Home Loan Bank has approved 110 new membership applications.

On the next slide you'll see that although we have those losses, you'll see that really the average size of our membership continues to increase. We've gone from in 2015, from an average member size of about $2.1 billion to $2.7 billion. What that illustrates is that although we've lost a number of charters, they have been mergers of what the Bank calls in-district, which means within our three-state territory. So, although we've lost a charter, our members have grown.

Mission asset activities

What we do next is show the number of members who are participating in our main programs, which are Advances, Letters of Credit, MPP and Housing. These numbers are not unique across all products. But, what I do want to point out is on that bottom in the italicized area, the fact that 80% percent of our members participate in a program, pretty consistently, and those numbers vary only from about 78% to about 81% over the last several years.

The Advance participation you can see has gone down the most and that ties in with what Andy talked about earlier on the drop in our Advance balances over the last several years. Letters of Credit, you see that number has been in fact increasing, and that program continues to see a lot of activity with a lot of members calling our Credit Operations group to talk about what that may mean for them.

MPP, although that number is dropping, is also a function of some member consolidation, mergers, so we've lost some activity there. And HCI – our Housing & Community Investment area – is obviously pretty consistent.

Credit products

What you see on the next slide is changes from year-over-year from March month-end '19 to March month-end '20. What this does illustrate is really the growth in two of our Advance products at a high level – short term and LIBOR – and really that was towards the end of March that were the result of the COVID-19 related borrowing from some of our members.

Advance rates

The next slide, obviously, with the movement in rates that both Andy and Dr. Mullineaux talked about, we believe the Advances are both an efficient and effective funding opportunity for the members and this chart certainly illustrates that there's been a compression in those spreads between other alternatives, maybe CD rates and things like that against our Advance rates offered to you, our membership.

LIBOR transition update

Andy mentioned the coming change with LIBOR. There's a lot of information out in the market. One source would be NewYorkFed.org. There's a lot of information on there to help you through or help with your better understanding of things that are going on with LIBOR. Andy mentioned that the target transition date remains December 31, 2021. The Financial Conduct Authority, and a lot of press you just see it listed as FCA, and the Bank of England have reiterated that the dates will not change. ARRC, which is the Alternative Reference Rate Committee and the Fed, has proposed SOFR as the substitution for LIBOR in the floating-rate space. Andy mentioned that the Home Loan Banks are the largest issuer of SOFR-related debt.

One of the questions is around the fact that SOFR is a risk-free rate and LIBOR had a credit component to it. So there's a group now called the Credit Sensitivity Group and it's highlighted in our document here, that is comprised of regulators, regional and community banks, to discuss adding some credit component to SOFR. And there's some information on that out there.

I will say that the Home Loan Bank of Cincinnati is not the only one working on LIBOR transition. It's a system effort. But you should know that the Cincinnati Bank has a representative on an ARRC committee.

Value delivered

Next, we always like to talk about delivering value to the membership. And really, we're starting from a position of strength. As Don mentioned, we were at 50-year lows in unemployment. We were at 20-plus-year lows in foreclosures throughout the industry or really the mortgage ecosystem as we could say, and 20-year lows on total delinquencies.

So, when you look at the predominant collateral type pledged to us, you see that's really one-to-four family residential mortgages on your books, and you see that about a third of the commercial real estate on our members' books are pledged. So there could be some more borrowing capacity there and I'll just go down to the Payroll Protection Program loans and I'm going to talk about more about that on the next page.

Payroll Protection Program loans as collateral

Andy mentioned the dates of the Home Loan Bank announcement, Cincinnati's announcement, being May 4 for our inclusion of the PPP loans as eligible collateral.

Also, just prior to that was an announcement by our regulator, the Federal Housing Finance Agency, on the parameters for allowing the banks to take those loans and they're listed here. You have to have a 4 or better credit rating with the Home Loan Bank and a CAMELS of 3 or better. No more than 20% of the member's borrowing capacity can be against PPP loans. No more than $5 billion in total can be pledged. And the haircut on those, or LVR, Lendable Value Rate, is 90%. There's some other information there. Also it's published in the Bank's credit policies.

Collateral changes in response to COVID-19

Other collateral changes that we've made in response to COVID-19 is a push out of LIBOR-linked collateral reporting. This gets to looking at the amount of LIBOR-related collateral on your books, and certainly any LIBOR collateral that may have final maturities past 12/31/2021.

Also we relaxed some of the parameters around modifications and those are also in our credit policy. We highlighted a few here that right now, modifications to loans on your books can be done electronically and within 60 days of the change, also modifications for deferrals and other payment terms. Also, an extension of the final maturity to 31 years from our standard 30 years.

FHLB moving toward eNote acceptance

Another collateral that we're looking at, that we hope to roll out, or will roll out in the second quarter of this year is the acceptance of eNotes as eligible collateral. I think I've mentioned this several times in these regional stockholder meetings, but I just reinforce that this has been about a two year project for, not only the Home Loan Bank System, Cincinnati, but also the industry, as a whole. When eNotes were originally designed and a lot of the legal agreements were formed, the concept was only a sale of eNotes between investors, not the concept of a pledge to a secured party, which certainly the Home Loan Bank is, as you leave the loan as earning assets on your books, but pledge them to us as eligible collateral. The one thing I want to note, in the discussion and documentation on this page is that the Bank put out an ECP, or eNote Collateral Pledge guide within the Collateral Guide. There's a lot of information in there. There are links to other standard industry information.

But one thing I do also want to point out is if you want to pledge eNotes to the Home Loan Bank as eligible collateral, there will need to be an addendum to the blanket security agreement before those become eligible.

Mortgage Purchase Program activity

I want to talk about MPP and the activity there. Obviously with where rates have gone, there's been a surge in activity, and I'll talk about that, but I do want to highlight a pretty consistent purchase volume of the program over the last several years.

I do want to point to the mandatory delivery contracts and for those of you who are PFIs, you recognize that that is your commitment to sell into the Home Loan Bank. You see that last year, we did just shy of 4,800, and all you guys can do the math – that turns out to be about 400 per month. Through April of this year, we're averaging about 900 MDCs per month. So obviously with where rates have gone, activity has picked up.

Another thing I want to point out is the contributions to your LRA, and you can see that's been pretty consistent in the $33 to $25 million dollar range. That LRA balance for the membership is slightly over a $330 million program to date. We have reimbursed our members for the credit quality of their loans, approximately $50-plus million in distributions with about $32 million additional being against claims, which minimizes our members' exposure under the MPP program. So that's a total of about $86 million returned to the PFIs, the sellers in this program.

You can see that on the bottom the number of PFI sellers, especially in the $1 billion and less and more focused in the $250 million dollar range has going down over the last several years. Again, that's a function of some mergers in the district; we've lost some of our smaller sellers.

MPP changes in response to COVID-19

I want to talk about the economy, not at Don's level. Certainly we've seen a long period of continuous improvements in the mortgage space, in the mortgage ecosystem as I called it earlier. We expect in the coming months and really into 2021, some credit deterioration and an increase in delinquencies. Obviously, we believe most of these are a function of COVID's impact on the economy and unemployment, or employment, whichever way you want to really look at that, and the implications for the industry is unfolding at a pace and scale really that's unprecedented. We firmly believe that over the next several months, we're really going to see what that impact is going to be.

That said, for PFIs and for those considering the program, you know that we just rolled out a new pool, new master commitment contracts, where we increased the required LRA, and that is a function of anticipating some higher delinquencies and some possible deterioration in the home price index.

As we've done with collateral, we've also made some changes for MPP in response to COVID relief , and that's relief as defined as verification of employment and appraisal relief for all mortgage applications dated prior to May 17. That mirrored Fannie and Freddie announcements. There's been an announcement this week that they've extended that, and I believe you'll see a notice from the Home Loan Bank that we may also extend that date.

Obviously there was a suspension of foreclosure sales and evictions for 60 days, and that date is May 25, reporting to credit bureaus on forbearance and payments and late fees and other things like that, authorized forbearance plans with up to six months' delay to reduce payments and the possible additional six months with Home Loan Bank approval. You'll note that we have been doing our best, being a portfolio investor, to follow industry leads, Fannie and Freddie being the dominant industry participation in changes.

Housing & Community Investment

And as far as Housing & Community Investment, obviously, Andy mentioned the RISE Program. That was a commitment of this Bank, voluntarily, of up to $2 billion with zero interest. I've talked to a number of members, and I commonly refer to that as free money. So hopefully many of our members can utilize that program. And also an expansion of our CIP and EDP programs. The Board authorized an increase of that to $1.5 billion and some relaxation of program parameters to make it easier for our members to utilize that for COVID-related borrowers and customers out in our district.

I would like to bring to your attention that in 2019 we celebrated the 30th anniversary of our Affordable Housing Program. During just 2019, 233 members participated in one or more of our housing programs, and just so you know, that's a little over 35% of our entire membership, so we think that's good utilization.

Through the competitive Affordable Housing Program, we did a record $30.9 million was awarded, and that really assisted with over 2,250 units of housing. In all, last year, we put out, we the Home Loan Bank, through our members $81.6 million, which I think speaks highly to our members and their commitment to their communities. Since the program's inception, the Bank has committed or disbursed, awarded, approximately $754 million to fund over 94,000 affordable housing units mostly in our district of Ohio, Kentucky and Tennessee.

2020 Financial Management Conference

Finally, I'd like to announce the 2020 Financial Management Conference. It's something we do every year and we're always excited about seeing our members and we appreciate your participation in that and your attendance.

It is scheduled for August 12-13 tentatively at the Hilton in downtown Cincinnati. You see the list of speakers there.

Obviously, if things change on our ability to hold this as an in person meeting, we will certainly let you know as early as possible. So, for your travel plans, right now, we are scheduled to go to a Reds game. But as you guys also know, right now, Major League Baseball is not playing games and really haven't come out with their plans for anything well into August, which is what this would be.

Typically right now, I'd ask a question, hold up a dozen Pro V1 golf balls for the correct answer, I'd give it to you as we would be headed out to the golf course. Andy did mention that his comments that we're still looking to reschedule our member appreciation events. Hopefully we'll be able to get those in late summer, early fall, so that we can in fact, see, our members as we so enjoy doing when we're out in the district.

Again, I want to thank you for your time, and I'm going to turn this back over to Andy.

Q&A

Andy: So with that, that concludes the presentations. We'll open it up to questions,

I do have a couple of questions asking if the slides will be available. They will be available on our website under Financial Results. But if you have trouble finding that, let us know, and we'll get that out to you, but it should be out on the website as we speak.

So Don, Kyle and myself will stay on the line here for a little while. We'll see if any questions come in.

Somebody asked if we could send a web link to the WEI website at the FRB (of New York), which I think was mentioned in our comments. We'll respond to that person specifically, or collectively if we can put something out on our website.

I do see some folks starting to drop off so before we get to any more, I want to express our appreciation for everybody taking some time to share with us today and express our sincere hope for the well-being of all of our members, your staff and the communities that you serve. We know you're vitally important to the communities and our economy. And our intention at the Federal Home Loan Bank is to support you as best we can in meeting those needs. So if there's anything that we can do, please reach out to us, your relationship manager, and the folks that you deal with on a daily basis here.

Somebody sent in and said on Bloomberg, the index is FRNYWEI7 Index GO, for those of you that have access to Bloomberg. So thank you for providing that.

Don: Andy, I see one question here, if the Fed goes back on their commitment to stay away from negative rates, what might compel them to do that?

I think that it's perfectly possible that long-term rates could be negative, while short term interest rates remain slightly positive. So the Fed doesn't have to take short-term rates into negative territory for the long-term rate to go negative.

All we really need is for people to get sufficiently, if they aren't already sufficiently panicked, to get even more so and start buying up Treasury securities like crazy, abandoning all other kinds of assets that could drive the longer term Treasuries into negative territory, while short rates are still positive.

Andy: We're getting a number of compliments coming in, so I won't share those. They're not necessarily questions, but thank you to those folks that are sending those nice comments into us.

We've got a question here, Don. You mentioned an article in the New Yorker. Could you repeat that article?

Don: I can. The article is from the May 11 issue of the *New Yorker*. And it is called "The Warnings." It's by a guy named David Quammen.

Andy: I've got another question here. The question is, has the 2.5% dividend rate ever been lower?

I did not go back and check over the years going back. I know at least probably since the early 2000s, it probably hadn't been below 4%, but I guess we also haven't had an environment where we've gotten down this low relative to interest rates and especially 10-year Treasury yields relative to what we talked about earlier. So I don't know going back further into that. Certainly something we can take a look at but at least from my recollection, I don't recall that going back to probably 2003 or so.

Here's another question regarding possible legislation.

I will say from a legislative standpoint that is moving quickly, and we'll see how this proposed legislation pops up relative to that. But we do have to be careful in terms of obviously, at this point, everybody is looking for sources of money. And it would be very easy to look at the Federal Home Loan Banks being owned principally by commercial banks and insurance companies and such from the financial industry to look at that as a source, whether it's to increase allocations we currently have or otherwise. So, it is something that as we find out more on that, or it progresses, and again, it can move very quickly, that may be something that we would reach out to you for assistance on, if there's representatives or senators in your particular area that would be helpful to the cause. We work very closely with the state trade groups in that respect, but it does get down to some individual relationships that are out there with our political representatives as well that are helpful.

OK, it's 11:17. We'll give it to 11:20 and then we'll call it a day, because I'm sure everybody's got things they can get back to.

I got a question here asking if any member has executed the PPP blanket agreement yet. I know we've got some pledges.

Kyle: Well, I didn't mention, although it's in the slide, that in order to pledge PPP loans they have to be listed and I believe there's about 10 pieces of data that have to come in with that listing. And it's a monthly listing of the loans, because we believe the balances will change.

Andy: So, as a part of that listing, it's an addendum to the blanket agreement to pledge those specific loans.

Andy: I would recommend that the person with that particular question, we'll have David Eastland reach out to you for that, or you can directly contact him with that particular question. But there's some additional documentation that goes with pledging that to the Federal Home Loan Bank, and Kyle explained some of the details in terms of that acceptance.

But, yes, we've had probably a handful of members that have pledged so far.

Okay, I've got 11:20, and no more new questions have popped up.

I would remind everybody, as I said earlier, we're on a limited staff in terms of what's here at the Bank, but everybody is working productively from home or our backup location.

If you've got any questions, reach out to us as you normally do, through either email or our toll-free numbers or direct lines. Everybody should be accessible. If you have any issues, let us know operationally, but hopefully, you're not experiencing any hiccups relative to that. We know you are also operating to some degree remotely as well, so we will work with you, in terms of making sure that everything works as smoothly as possible.

But again, unprecedented environment, and everybody trying to move forward in a positive way.

So, thank you all. Everybody be safe and be well, and thanks for joining us today, and we hope to see you soon in person, either at the August meeting, if we're able to do so by then, or at the member appreciation outings, when we schedule those. So, let's be hopeful and optimistic that we're able to do that in a couple of months towards the end of the summer.

So, with that, I'll say, thank you and goodbye to everybody.

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