PRESS RELEASE

Federal Deposit Insurance Corporation

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Media Contact:
Rosemary George (202) 898-6530

FDIC SAYS RECENT VOLATILITY IN LONG-TERM INTEREST RATES MAY CONTINUE

FOR IMMEDIATE RELEASE

The FDIC today said that several related factors have contributed to an upward trend in the volatility of long-term U.S. interest rates, and that these factors could cause continued volatility going forward. According to a report released today in the Winter 2003 ***FDIC Outlook***, concerns about deflation, mortgage-related hedging activity, dependence on foreign capital and a rising federal budget deficit have all played a role in recent interest rate movements. "In this somewhat more volatile interest-rate environment, the FDIC is continuing to monitor the potential impact that rising rates might have on the earnings of insured depository institutions," said FDIC Chairman Don Powell.

FDIC analysts say that the level of volatility during the summer of 2003 was unusually high by historical standards, particularly given the absence of major events or economic shocks. After reaching a 45-year low on June 13, the yield on 10-year Treasury instruments soared by more than 120 basis points over the next 45 days.

While a gradually strengthening economy might be expected to put upward pressure on interest rates, it appears that the recent bout of volatility may not be entirely related to improving economic fundamentals. Instead, the historically low level of interest rates in May and June, combined with concerns about the possibility of deflation, appears to have set the stage for a period of unusually large interest-rate swings in late June and July.

Congress created the Federal Deposit Insurance Corporation in 1933 to restore public confidence in the nation's banking system. It promotes the safety and soundness of these institutions by identifying, monitoring and addressing risks to which they are exposed. The FDIC receives no federal tax dollars — insured financial institutions fund its operations.

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According to the report, hedging activities by mortgage lenders probably added to the size of recent interest-rate movements, as did increases in official estimates of the federal budget deficit. While foreign purchases of dollar-denominated assets have helped keep U.S. interest rates low, dependence on foreign capital could itself become a source of interest-rate volatility should these capital flows be suddenly reversed. FDIC analysts expect that, to the extent that these causal factors remain in place, long-term U.S. interest rates could remain volatile compared to historical norms.

The interest-rate environment is a major consideration in the earnings outlook for FDIC-insured banks and savings institutions. During a historically low interest-rate environment, FDIC-insured institutions recorded record-high earnings in 2002 and the first two quarters of 2003. Today's ***FDIC Outlook*** also addresses a variety of regional developments including:

Atlanta Region. The housing sector is a key earnings driver for many of the Region's commercial banks, and recent increases in residential mortgage rates could challenge revenue streams.

Chicago Region. The Chicago metro area economy and banking market are large and diverse. The economy has underperformed the nation in recent years, and competition for the retail banking business is strong and intensifying.

Dallas Region. Strong demand and tight supplies are keeping natural gas prices high, benefiting regional gas producers, but hindering farmers and manufacturers that rely heavily on consumption of natural gas.

Kansas City Region. Drought in the Region's western states significantly reduced net farm income in 2002. Farm banks based in areas of persistent drought are now reporting rising delinquencies and increased levels of carryover debt.

New York Region. Historically, a steeper yield curve has been positive for bank margins. However, the recent rise in interest rates may challenge the Region's banks holding high concentrations of long-term assets.

San Francisco Region. Record levels of mortgage prepayments have reduced mortgage servicing asset values. Interest-rate increases may boost servicing values, but could heighten levels of extension and credit risk.

FDIC Outlook—Winter 2003 Edition