PRESS RELEASE

Federal Deposit Insurance Corporation

March 2, 2004

Media Contact:
David Barr (202) 898-6992

FDIC Study: Implications of Housing Market Boom

FOR IMMEDIATE RELEASE

In a report issued by the Federal Deposit Insurance Corporation (FDIC) today, analysts conclude that the recent boom in U.S. home prices and housing market activity does not necessarily imply that prices are poised to systematically decline. However, the report does cite the rising use of home equity lines of credit and adjustable-rate mortgages as factors that could make some homeowners more vulnerable to credit problems. According to the Spring 2004 issue of *FDIC Outlook*, homeowners who are highly leveraged or exposed to higher interest rates could face problems, even in an improving economy, leading to potentially higher loss rates in mortgage loan portfolios in the event of rising interest rates or declining local home prices.

Today's report discusses recent concerns among some economists that a possible nationwide housing bubble may be developing on the heels of robust activity in the housing sector and mortgage markets in recent years. Low interest rates have spurred strong demand for housing, rising rates of homeownership, record refinancing activity, and large increases in mortgage indebtedness. But FDIC analysts find that the inherent attributes of homeownership serve to make housing less vulnerable to sudden price declines compared to other assets such as equity shares. Because home prices are primarily influenced by local economic and demographic factors, significant price declines have occurred historically only in markets experiencing serious economic distress. The report concludes that a widespread decline in home prices appears unlikely, even when mortgage rates begin to rise from current low levels.

However, risks remain in mortgage portfolios dominated by highly-leveraged borrowers with volatile incomes or limited financial reserves. Subprime borrowers and homebuyers in high-priced home markets tend to rely heavily on adjustable-rate mortgages, leaving them vulnerable to rising debt service costs once short-term interest rates begin to rise.

Today's *FDIC Outlook* also addresses a variety of regional developments including:

Atlanta Region: Structural and cyclical forces are set to affect the performance of the manufacturing sector. Areas with significant employment in traditional industries (such as textiles and furniture) that remain under structural pressure may recover more slowly than emerging industries (such as computers, electronics, and transportation equipment), and the credit quality of insured institutions could weaken further.

Chicago Region: The regional economy is improving, albeit unevenly among industries and across states. If interest rates rise further, insured institutions will face continued challenges to increasing revenue while maintaining favorable asset quality.

Dallas Region: Branching activity in the region, driven by economic and demographic factors, has significantly exceeded the national average during the past decade. Performance of insured institutions varies depending on response to specific branching strategies.

Kansas City Region: Drought conditions may begin to have an impact on farmers' ability to irrigate crops, which could hurt yields and contribute to greater weakness in agricultural bank credit quality.

New York Region: The housing sector continued to perform strongly in the Northeast. However, higher interest rates and moderating appreciation in home prices could challenge the region's insured institutions.

San Francisco Region: Despite weak office market fundamentals, such as prolonged job losses and high vacancy rates, insured institutions in several metropolitan areas report exposures to commercial real estate lending that exceed the national median. Credit quality remains sound overall; however, continued economic weakness could contribute to deterioration in asset quality going forward.

[FDIC Outlook]