Evaluation of Municipal Securities

I. Overview & Industry Trends

Overview of Presentation

Overview & Industry Trends

Investment Policies & Procedures

Basic Analysis

Expanded Analysis

Review & Additional Resources

Recent Regulatory Changes

The Dodd-Frank Act required regulators to remove references to ratings provided by rating agencies from regulations.

In 2012, the OCC & FDIC issued Final Rules and Guidance addressing alternatives to the use of external credit ratings.

Banks cannot rely solely on credit ratings to determine creditworthiness.

Supervisory Expectations

Market Characteristics

- Size of market: $3.7 Trillion
- Average annual issuance: $381.2 Billion
- Majority of new issuances are under $10 Million
- Number of bonds outstanding: > 1 Million
- Number of issuers: > 89 Thousand

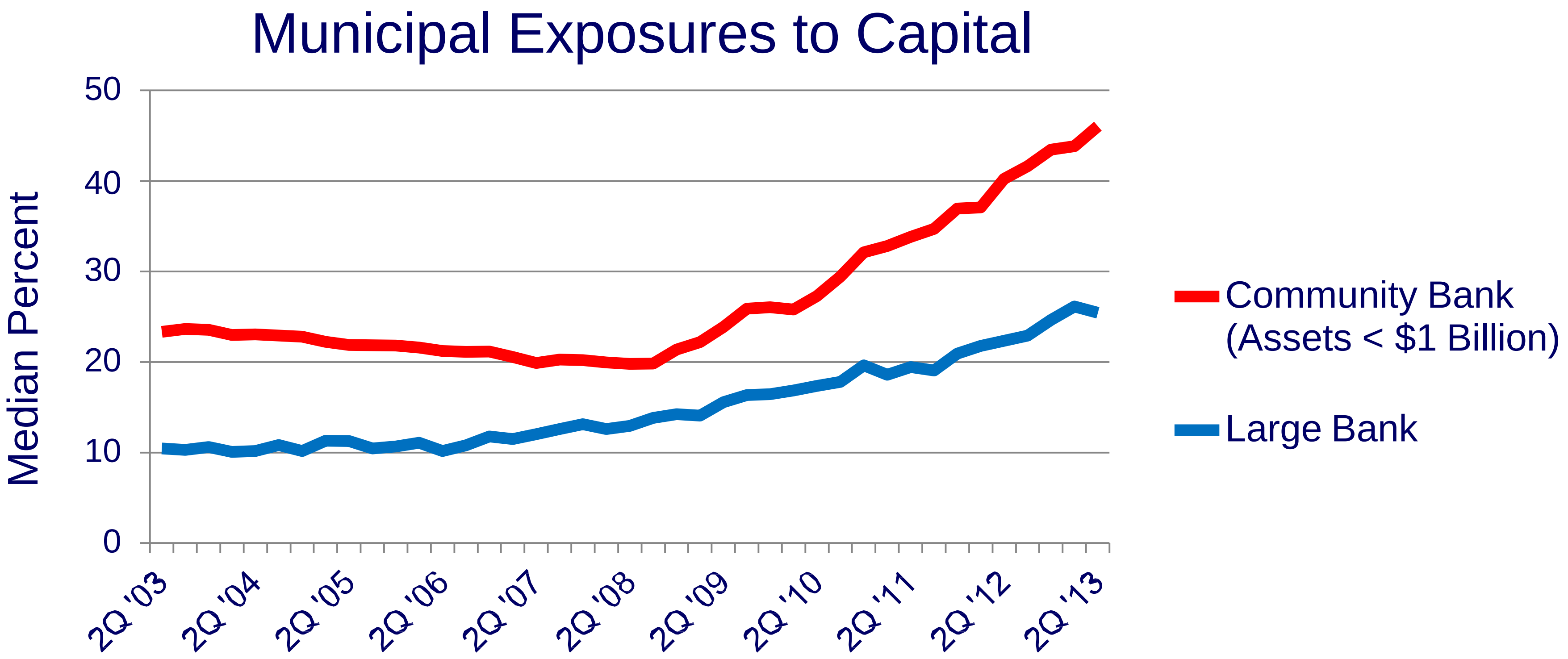
As of December 31, 2012

Source – Federal Reserve, EMMA, SEC, 2012 Census of Governments

Challenges in Assessing Credit Risk

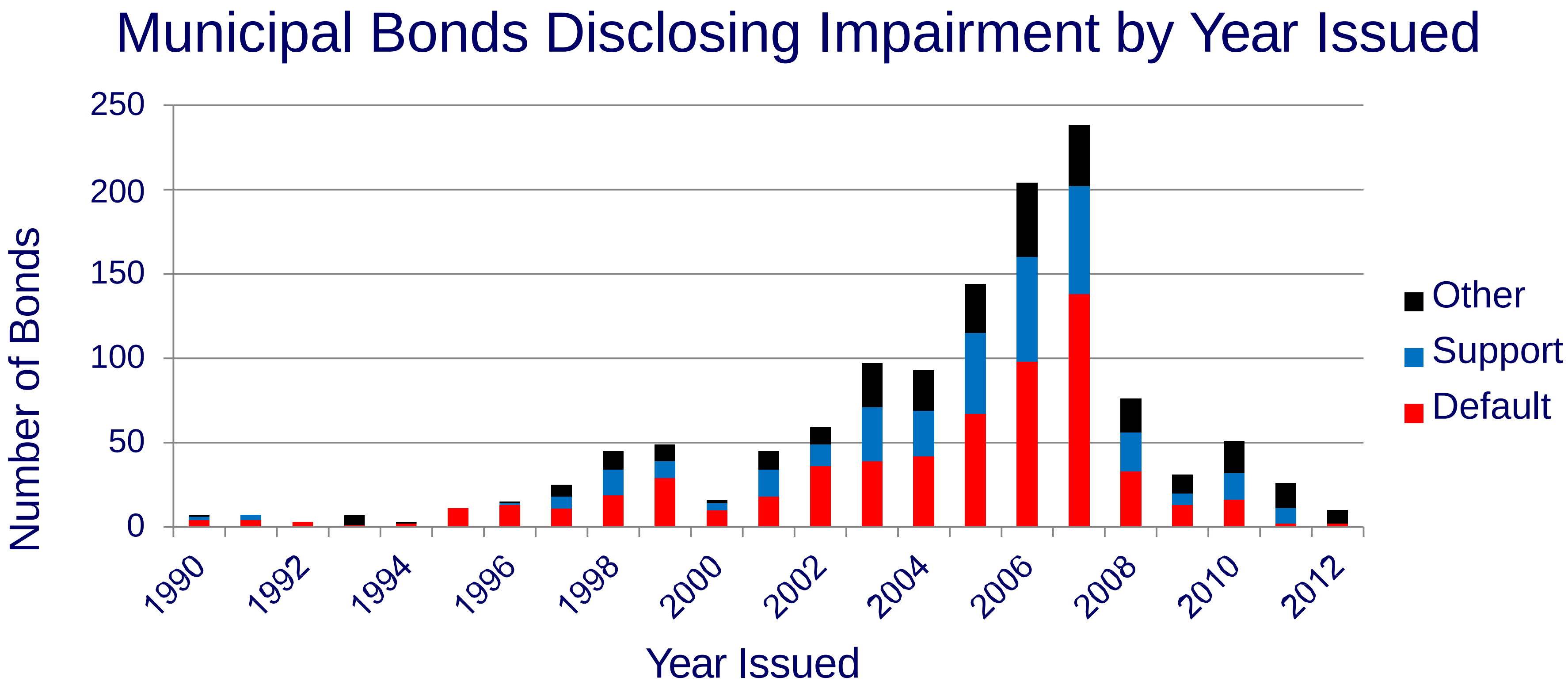
- Untimely financial information
- Different accounting standards (GASB vs. FASB)
- Unfunded pension and other postemployment benefit obligations
- Legal uncertainty
- State-specific bankruptcy laws

Bank Median Exposures to Municipalities



Source – Call Report Data

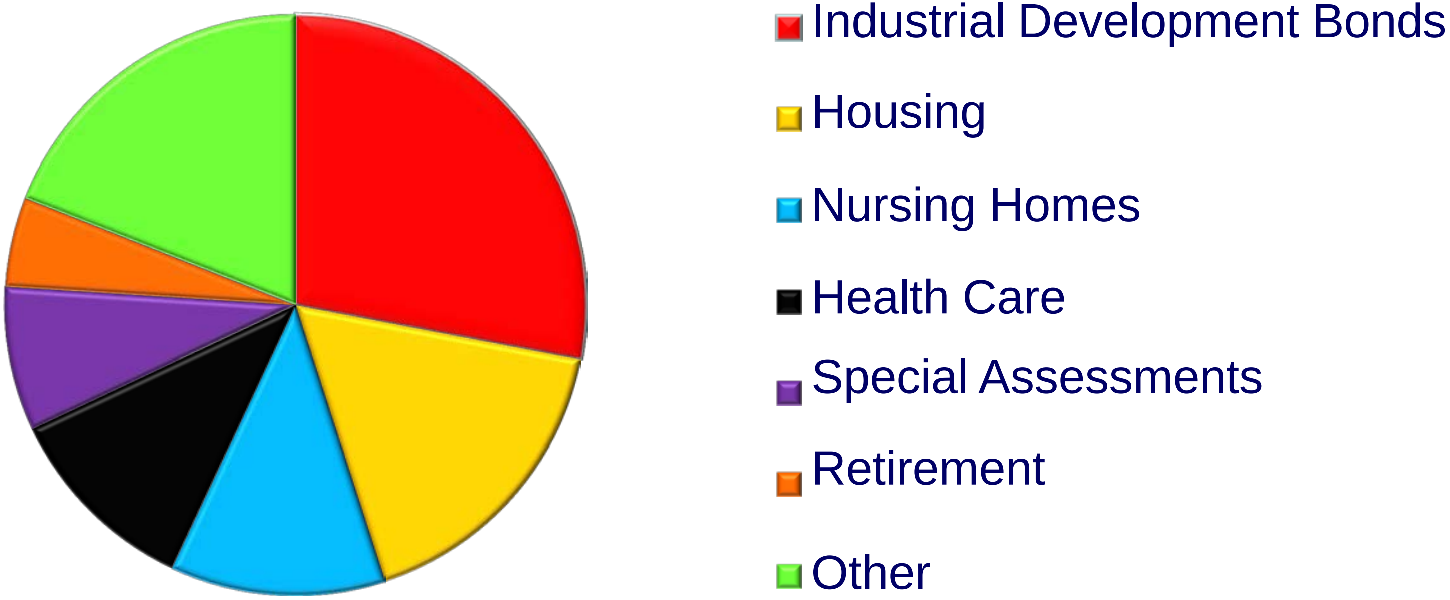
Vintage Analysis



Source – Municipal MarketAdvisors

Municipal Bond Historical Defaults

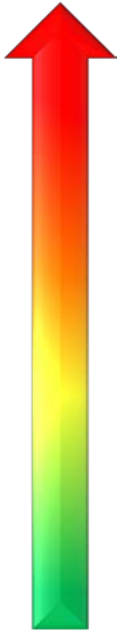
Defaults (1958-2011)



Source – Federal Reserve Bank of New York

Credit Risk by Type of Municipal Issuance

Higher Risk



Lower Risk

- Other Municipal Issuances
- Non-Essential Purpose Revenue Obligation Bonds
- Essential Purpose Revenue Obligation Bonds
- General Obligation Bonds

Summary

- Banks should have a process to determine whether investments satisfy creditworthiness standards
- Banks cannot rely exclusively on external credit ratings to determine creditworthiness
- Supervisory expectations are based on the exposure level and risk profile of the portfolio