Federal Deposit Insurance Corporation
550 17th Street NW, Washington, DC 20429
Division of Insurance and Research

November 15, 2004

MEMORANDUM TO: The Board of Directors

FROM: Arthur J. Murton, Director
Division of Insurance and Research

SUBJECT: SAIF Assessment Rates for the First Semiannual Assessment Period of 2005

Recommendation

The staff recommends that the Board maintain the existing Savings Association Insurance Fund (SAIF) assessment rate schedule of 0 to 27 basis points (bp) [1] per year. This rate schedule complies with the statutory requirements of the Federal Deposit Insurance Act for the Board to establish a risk-based assessment system and set assessments only to the extent necessary to maintain the SAIF at the Designated Reserve Ratio (DRR) of 1.25 percent.

Concur:

William F. Kroener, III
General Counsel

[1] Although the current effective rate schedule is 0 to 27 basis points, the base rate schedule, established in 1995, is still 4 to 31 basis points. The FDIC may alter the existing rate structure and may change the base SAIF rates by rulemaking with notice and comment. Without a notice-and-comment rulemaking, the Board has authority to increase or decrease the effective rate schedule uniformly up to a maximum of 5 basis points, as deemed necessary to maintain the target DRR.

Summary

Staff believes that the SAIF reserve ratio will remain above the DRR throughout the assessment period. Therefore, staff recommends maintaining the existing assessment rate schedule. Based on June 30, 2004 data and projected ranges for the relevant variables at June 30, 2005, this rate schedule would result in an average annual assessment rate of approximately 0.06 basis points (bp).

Staff has considered a range of plausible events that could produce significant movements in the SAIF reserve ratio. Our methodology provides ranges for estimated insurance losses that are primarily based on estimated changes to the contingent liability for anticipated failures (contingent loss reserve), changes in both interest income and in the market value of available-for-sale (AFS) securities resulting from changes in interest rates, and growth of insured deposits.

ANALYSIS

In setting assessment rates since the recapitalization of the SAIF, the Board has considered: (1) the probability and likely amount of loss to the fund posed by individual insured institutions; (2) the statutory requirement to maintain the fund at the DRR, currently 1.25 percent, and (3) all other relevant statutory provisions.[2]

[2] The Board reviews and weighs the following factors when establishing an assessment schedule: a) the probability and likely amount of loss to the fund posed by individual institutions; b) case resolution expenditures and income; c) expected operating expenses; d) the revenue needs of the fund; e) the effect of assessments on the earnings and capital of fund members; and f) any other factors that the Board may deem appropriate. These factors directly affect the reserve ratio prospectively and thus are considered as elements of the requirement to set rates to maintain the reserve ratio at the target DRR.

Projections for the SAIF Reserve Ratio over the Next Assessment Period

Staff's best estimate for the SAIF reserve ratio as of June 30, 2005 is 1.34 percent. The lower and upper bounds of the likely range for the SAIF reserve ratio as of June 30, 2005 are 1.28 percent and 1.40 percent, respectively. The lower bound of the estimated range exceeds the statutory requirement of 1.25 percent.

The following is an analysis of the anticipated effect of changes in the fund balance and the rate of insured deposit growth on the projected reserve ratio as of June 30, 2005.

1. Fund Balance

Staff evaluates three significant inputs in estimating changes to the fund balance. First, staff estimates the impact of probable insurance losses, which are primarily losses from failed institutions. Second, staff estimates the amount of interest income that the fund will receive through June 30, 2005. Third, staff projects the level of unrealized gains and losses on available-for-sale (AFS) securities through June 30, 2005.

A. Insurance Losses

Insurance losses primarily consist of two components: a contingent liability for anticipated failures (contingent loss reserve) and an allowance for losses on institutions that have already failed. The Financial Risk Committee (FRC) recommends the amount of the contingent loss reserve each quarter. This recommendation represents the FRC's best estimate of "probable and estimable" SAIF losses from potential institution failures, as required by generally accepted accounting principles. Actual results could differ from these estimates. As of June 30, 2004 the

SAIF loss reserve stood at $2 million. The SAIF loss reserve increased to $10 million as of September 30, 2004.

Staff has estimated a likely range of insurance losses based on projected changes in the contingent loss reserve for the period ending June 30, 2005. These projections are influenced by several factors, including: (1) the shifting of problem institutions among different risk categories within the reserve, (2) the reduction in problem institutions due to improved financial conditions, mergers, or failures, and (3) the addition of new problem institutions. To capture the effects of these changes, staff uses a migration approach, which estimates the probabilities of institutions entering into or leaving the contingent loss reserve as well as the probability of institutions moving between loss reserve risk categories. These probabilities are based on the recent history of changes to the reserve. Other factors driving changes in the contingent loss reserve are changes in expected failure rates and changes in rates of loss in the event of failure. For purposes of estimating the contingent loss reserve, staff assumes that failure and loss rates remain constant through the period.

Based on consideration of the above factors, staff estimates that potential loss provisions for failures for the twelve months ending June 30, 2005 will range from $4 million to $142 million, with a best estimate of $42 million.[3] Table 1 shows the range of potential loss provisions for failures as well as adjustments for net losses/recoveries on resolution receivables, and adjustments for litigation losses.

[3] Staff estimates that the balance of the contingent loss reserve as of June 30, 2005 will range from $7 million to $130 million, with a best estimate of $39 million.

Table 1
Potential Provisions and Adjustments for Loss Allowances
For the Twelve Months Ending June 30, 2005

	Low (High Provision) Estimate	Best Estimate	High (Low Provision) Estimate
Provision Related to Future Failures (1)	$142 million	$42 million	$4 million
Adjustment for Closed Institutions' Net Recoveries (2)	$28 million	$14 million	$0
Adjustment for Litigation Losses (3)	$3 million	$0	-$3 million
Potential Provision for Losses*	**$173 million**	**$56 million**	**$2 million**

* Figures may not add to totals due to rounding.

Notes:

(1) Includes provisions required to bring the contingent loss reserve to estimated June 30, 2005 levels after accounting for a) actual reserve losses sustained in the third quarter of 2004 ($0) and b) estimated losses sustained through June 30, 2005 ($6 million under the Best Estimate). Changes in the contingent loss reserve occur because of failures, mergers, improvement in problem institutions' conditions, deterioration of existing problem institutions, and new problem institutions.

(2) Estimates include a third quarter 2004 increase of $14 million in estimated losses on prior failures. Low and high estimates assume a range around the best estimate of -5% to +5% of the estimated net recovery value of institution resolution receivables totaling $274 million as of June 30, 2004.

(3) Range is based on the standard deviation of changes in the year-end contingent liability for litigation losses for the period 1998 to 2003.

Staff believes that the range provided by the statistical migration analysis adequately represents the most likely range of additional provisions needed to cover insurance losses from future failures. However, the bounds of this range do not represent "best case" and "worst case" scenarios, and larger or smaller provisions could occur.

FDIC staff economists, working with academic researchers, have developed and are currently refining an alternative approach to measure risks posed to the insurance funds. This approach, referred to as the Loss Distribution Model or LDM, employs many of the same techniques and methods used in credit risk and economic capital models employed by large financial companies to measure and manage risk. The LDM provides estimates of failure-related

losses that are most likely given current industry conditions, as well as failure-related losses that might result from changes in the condition of the economy and the industry.[4]

Using the LDM, staff developed alternative SAIF loss provisions related to future failures for the 12 months ending June 30, 2005 that range from -$2 million to $148 million, with a best estimate of $78 million that represents the mean of the LDM-produced distribution of possible losses. These results are close to those of the statistical migration analysis shown in Table 1 and lead to a similar projected range (and best estimate) for the reserve ratio as of June 30, 2005.

SAIF-insured institutions in general appear to be well positioned to withstand considerable financial stress from unlikely economic shocks. Staff has considered economic stress events as they relate to specific risk concerns enumerated in the industry outlook contained in Tab 1. To determine the potential insurance fund implications of these concerns, staff has developed several stress event simulations, each of which demonstrates that SAIF-insured institutions are well positioned to withstand a significant degree of financial adversity.

Subprime Lending Risk: Staff believes that subprime lending continues to be the most likely source of near-term losses to the insurance funds. Subprime lenders make up 36 percent of the assets of institutions on the contingent loss reserve list.

[4] The failure component of the model estimates the probability of failure for each insured institution using a statistical approach based on predictive variables such as examination ratings, problem asset ratios, capital levels, and profitability measures. The loss component estimates the loss-given-failure based on historical loss experience, the types of assets held, and the liability structure (priority of receivership claims) of each individual institution. The deposit growth component estimates deposit levels in each insured institution based on previous deposit growth rates, examination ratings, and quarters-in-existence. These three components produce initial period parameter estimates of failure probabilities, losses, and deposit exposures. The economic component of the model then forecasts changes in these parameters using statistical relationships between the parameters and changes in economic variables, including the term structure of interest rates, regional and national bank stock price indices, and regional house price indices. Finally, a computer simulation using a wide variety of different economic scenarios produces a distribution of possible failures and related insurance fund losses, which are discounted back from the time of failure to the present time.

Using periods of historically poor performance for various categories of consumer loans, staff subjected subprime lending institutions to instantaneously higher consumer loan loss rates sustained for two years. Based on data from the second quarter of 2004, these simulations produced failed SAIF-insured institution assets of only $0.3 billion (less than one tenth of 1 percent of institution assets considered). Simulations using data from a year earlier resulted in a level of failed assets of $1.6 billion.

Mortgage Lending Risk: Prospects for rising interest rates may cause some concern over the future performance of institutions engaged in mortgage lending activities. Rising rates could place pressure on the net interest margins of some mortgage lending institutions by raising funding costs against fixed-rate loan portfolios and securities holdings. Higher rates could also suppress mortgage origination volumes and the value of home prices in the face of weaker sales activity.

Using periods of historically significant declines in both net interest margins and mortgage loan performance, staff subjected institutions with mortgage lending concentrations to a two-year period of higher loan loss rates and declining net interest margins. Based on data from the second quarter of 2004, these simulations produced failed SAIF-insured institution assets of only $0.2 billion (one twentieth of 1 percent of institution assets considered). Simulations using second-quarter 2003 data resulted in failed assets of $0.9 billion.

Commercial Real Estate Mortgage Lending Risks: Rising interest rates could also have an adverse impact on commercial real estate loan performance as debt servicing burdens on variable rate loans increase. Institutions with heavy commercial real estate loan concentrations are most vulnerable to any rise in commercial real estate loan losses.

Using periods of historically significant declines in commercial real estate values, staff subjected institutions with commercial real estate mortgage lending concentrations to a two-year period of higher loan loss rates. Based on data from the second quarter of 2004, the worst case simulation, which drew on the experience of New England institutions during the late 1980s, produced failed SAIF-insured institution assets of $1.1 billion over two years (0.7 percent of institution assets considered). Results using data from a year earlier were similar. By contrast, this same simulation produced just under $8 billion in failed SAIF-insured institution assets using year-end 1991 data.

Based on these findings, combined with signs of improving overall economic conditions, staff believes that widespread deterioration in thrift industry performance is unlikely in the next one-to-two years.[5] However, if the stress conditions described above were to persist beyond a two-year horizon, it is possible that the effects on bank performance could be more severe. Furthermore, the historical experiences underlying the stress scenarios may be less applicable in the future. For example, greater "democratization" of credit, larger securitization volumes, and higher household debt levels in recent years could have altered the magnitude of stress on bank conditions from potential future problems in residential mortgage or commercial real estate sectors. Thus, conclusions drawn from the stress scenario analyses should be treated with some degree of caution.

B. Interest Income and Unrealized Gains and Losses on AFS Securities

Staff relied upon expert forecasts as detailed in the *Blue Chip Financial Forecasts* to develop interest rate projections and analyze the potential effect of changes in interest rates on

[5] Staff also simulated the effects of a historically-derived stress scenario on current non-real-estate commercial and industrial (C&I) loan specialists. However, there are only 7 SAIF-insured C&I specialists, and simulation results indicated that none would fail under the stress scenario.

interest income and unrealized gains and losses on AFS securities. The forecasts defined as our "best estimate" were the consensus forecasts through the second quarter of 2005 as detailed in the September issue of the *Blue Chip Financial Forecasts*. Adopting the experts' consensus forecasts also allows for forecasted yield curves that change in shape over time.[6]

Along with forecasting yield curves based upon the experts' forecasts, staff also calculated upper and lower bounds for interest rates using the historical differences between the experts' forecasts and the actual interest rates. These bounds vary over the assessment period and change in shape over time, as opposed to being parallel shifts in rates. The bounds are consistent with the notion that the projections represent the most likely scenarios and that the actual rates may be above or below the projections. In general, the projections indicate rising rates for the period under consideration. Charts showing the projected rates, upper bound, and lower bound are included as Appendix A to this case.

Table 2 shows projections for low, best, and high estimates for interest income and unrealized gains and losses on AFS securities using the forecast rates and upper and lower bounds.[7] Because of the significant percentage of AFS securities held in the insurance fund portfolio at this time, when interest rates change, the magnitude of the resulting change in market value of these securities dominates the effect of changes in interest income.

[6] Staff also developed alternative interest rate projections using actual forward rates available as of approximately the same time that the projections in the September *Blue Chip Financial Forecasts* were generated.. Forward rates are yields on future securities of varying maturities derived from the term structure of interest rates. (The term structure of interest rates refers to the relationship between yields on comparable securities but different maturities.) Staff developed upper and lower bounds using historical differences between actual interest rates and corresponding forward rates. The projections using forward rates were similar to the *Blue Chip* experts' consensus forecasts and result in a projected range and best estimate for the reserve ratio as of June 30, 2005 that are very similar to the results using the *Blue Chip* projections.

[7] The projections incorporate actual results for the third quarter of 2004.

Table 2

Potential Interest Income and
Unrealized Gains (Losses) on AFS Securities
June 30, 2004 to June 30, 2005 ($ in millions)

	Low Estimate (1)	Best Estimate (1)	High Estimate (1)
Interest Income	545	537	528
Unrealized Gain (Loss) on AFS Securities (2)	-173	-93	-10
Net Fund Contribution from Investment Activities	**372**	**444**	**518**

Notes:

(1) The Low Estimate is calculated using upper bound interest rates, the Best Estimate is calculated using the projected rates, and the High Estimate is calculated using the lower bound rates. Because the level of interest rates is assumed to be generally higher in the Low Estimate than in the other two, overall interest revenue is also higher in that scenario. However, the Low Estimate also assumes more failures and higher resolution outlays, which results in a smaller balance invested during the period and partially offsets the effect of higher interest rates on investment income.

(2) Figures include actual investment income and unrealized gains/losses on AFS securities for the third quarter of 2004 and projected investment income and gains/losses for the remaining period through June 30, 2005.

Staff's best estimate reflects recent trends in market interest rates as well as expert forecasts. Short-term Treasury yields have increased since May as the Federal Reserve raised the target for the federal funds rate by 100 basis points. Long-term Treasury yields declined during the same period amid concerns over rising oil prices, weaker consumer spending and lackluster job reports. Despite this recent decline in long-term interest rates, experts continue to forecast a gradual increase in long-term Treasury yields, accompanied by a slightly sharper increase in short-term yields over the nine-month period ending in June 2005 as the economy regains its momentum. Some depreciation in the value of AFS securities should be expected if interest rates rise at a pace similar to staff's best estimates. As the remaining maturity of the existing AFS portfolio shortens, previously identified unrealized gains will also dissipate. Over the longer term, higher yields on Treasury securities will boost overall interest earnings as securities reprice upward and as maturing securities are reinvested at higher rates.

C. Projected Fund Balance

Table 3 summarizes the effects on the fund balance of the low, best, and high estimates assumed for insurance losses, interest income, and unrealized gains and losses on AFS securities. The projection also assumes that the current assessment rate schedule will remain in effect through June 30, 2005.

Table 3
Projected Fund Balance (1)
($ in millions)

	Lower Bound	Best Estimate	Upper Bound
Assessments (2)	7	7	7
Interest Income (3)	545	537	528
Total Revenue	552	544	535
Operating Expenses (4)	136	136	136
Provision for Losses	173	56	2
Total Expenses & Losses	309	192	138
Net Income	243	352	397
Unrealized Gain (Loss) on AFS Securities (3)	-173	-93	-10
Comprehensive Income (Loss) (5)	70	259	387
Fund Balance – 6/30/04	12,411	12,411	12,411
Projected Fund Balance – 6/30/05	12,481	12,670	12,798

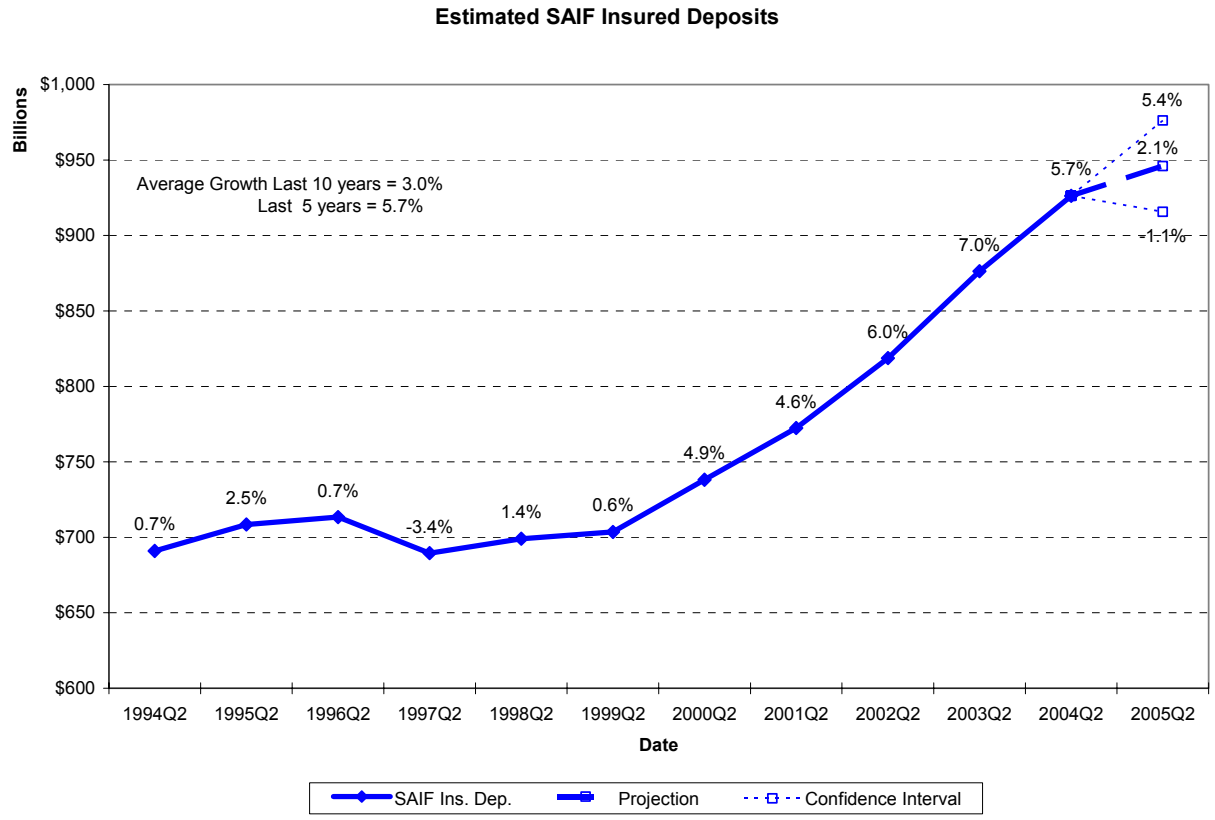
Notes:
(1) Projected income and expense figures are for the twelve months ending June 30, 2005.
(2) Assumes that the current assessment rate schedule remains in effect through June 30, 2005.
(3) See notes to Table 2 for an explanation of changes in interest revenue and unrealized gains (losses) on AFS securities under these projections.
(4) Projected operating expenses are based on estimates of expenditures for the second half of 2004 and preliminary budget projections for the first half of 2005. Expenses are allocated across FDIC-managed funds based on the allocation of actual 2003 expenses for budgeted items.
(5) Comprehensive Income is used instead of Net Income due to the magnitude of the change in market value of AFS securities that occurs with fluctuations in interest rates. See note (3) above.

2. Insured Deposits

Figure 1 shows that SAIF-insured deposit growth rates since 1994, measured as of June of each year from the previous June, have been as high as 7.0 percent and as low as -3.4 percent.

After positive growth rates of 0.7 percent, 2.5 percent, and 0.7 percent in 1994, 1995, and 1996, respectively, SAIF-insured deposits declined 3.4 percent in 1997. Following modest growth in 1998 and 1999, SAIF-insured deposits increased at a significantly faster pace, with annual growth rates ranging between 4.6 percent and 7.0 percent, through June of this year.

Figure 1



Staff's best estimate for insured deposit growth over the four quarters from June 2004 through June 2005 is 2.1 percent. The estimate takes into account the likely slowdown in deposit growth due to an expected rise in long-term interest rates, which may make alternative investment opportunities more attractive than bank deposits.

It takes approximately $7 billion in insured deposit growth to reduce the SAIF reserve ratio by 1 basis point. Based upon the June 30, 2004 fund balance, it would take an increase of $66.7 billion in SAIF-insured deposits (7.2 percent growth) to reduce the reserve ratio to the

DRR of 1.25 percent, all else being equal. The staff's best estimate indicates that deposit growth over the next four quarters will be significantly lower than this figure.

Based on projections using a statistical model, the best judgment of the staff is that SAIF-insured deposits are likely to experience a growth rate in the range of -1.1 percent to +5.4 percent between June 2004 and June 2005.[8] Staff believes the most likely scenario is that insured deposits will grow at the midpoint of this range (2.1 percent), which will bring the total for SAIF-insured deposits to $946 billion. Future conditions that could result in insured deposit growth at the high end of the range of our forecast may include a depressed stock market with high volatility. In contrast, a rising stock market and strong U.S. economic growth could result in insured deposit growth at the low end of the range of the forecast.

3. SAIF Reserve Ratio

Based on the projected SAIF balance and the growth of the insured deposit base, the best estimate of the SAIF reserve ratio at June 30, 2005 is 1.34 percent (Table 4). The best estimate assumes modest loss provisions for future failures, moderately rising Treasury yields, and insured deposit growth of 2.1 percent over the four quarters ending June 30, 2005.

Staff projects the lower bound and upper bound of the likely range to be 1.28 percent and 1.40 percent, respectively (Table 4). The lower bound, which reflects a 6 bp decrease from the June 30, 2004 ratio, assumes a strong increase in the insured deposit base (5.4 percent growth) and higher interest rates that reduce the fund balance by raising unrealized losses on AFS

[8] The model is a regression model where the current growth rate in insured deposits is estimated as a linear function of the previous growth rate in insured deposits, the current and previous growth rates of total (insured and uninsured) domestic deposits, as well as the current yields on 3-month Treasury bills and 10-year Treasury notes. The range corresponds to a 95% confidence level. In other words, if the process generating insured deposit growth in the future is the same as in the past, we can be sure with 95% confidence that the actual growth rate in insured deposits, over the year 2004, will lie within this range. The growth rate predicted by the model (thus, the most likely rate) is the midpoint of this range.

securities (Table 3). The lower bound also incorporates the high insurance loss estimate as projected by staff. Although the estimate reflects staff's view of a reasonably possible adverse scenario, it is not intended to represent a "worst case" scenario.

The upper bound produces a 6 bp increase in the reserve ratio relative to June 30, 2004 levels. This estimate assumes a contraction of 1.1 percent in the SAIF-insured deposit base, very low provisions for failure-related losses, and a more modest increase in interest rates, which results in smaller unrealized losses on AFS securities.

Table 4
Projected SAIF Reserve Ratios
($ in millions)

	June 30, 2004		
Fund Balance	$12,411		
Estimated Insured Deposits	$926,198		
SAIF Ratio	1.34%		
	Lower Bound (1) June 30, 2005	**Best Estimate (2) June 30, 2005**	**Upper Bound (3) June 30, 2005**
Projected Fund Balance	$12,481	$12,670	$12,798
Estimated Insured Deposits	$976,072	$945,900	$915,726
Estimated SAIF Ratio	1.28%	1.34%	1.40%

Notes:
(1) The Lower Bound refers to the scenario of higher loss provisions (Low Estimate in Table 1), the higher end of the range for interest rates (Low Estimate in Table 2), and insured deposit growth of 5.4 percent.
(2) The Best Estimate refers to a baseline scenario of moderate loss provisions (Best Estimate in Table 1), moderately rising interest rates (Best Estimate in Table 2), and insured deposit growth of 2.1 percent.
(3) The Upper Bound refers to the scenario of lower loss provisions (High Estimate in Table 1), the lower end of the range for interest rates (High Estimate in Table 2), and a 1.1 percent decline in insured deposits.

Staff's best estimate of the reserve ratio for June 30, 2005 is 9 bp higher than the DRR and unchanged from the ratio at June 30, 2004. The most significant factor influencing the stability of the reserve ratio is projected modest insured deposit growth, which helps to offset other factors that would tend to place downward pressure on the ratio, including the following:

- Interest rates remain at very low levels but have begun to move higher in line with improving economic conditions. Unrealized gains on AFS securities will decline even in a stable interest rate environment because these gains disappear as securities move closer to their

maturity dates. With rates moving higher, reductions in unrealized gains (or increases in unrealized losses) can be expected to accelerate.

- Although staff remains optimistic about industry prospects, reserves for anticipated losses are already at low levels, precluding substantial reversals to loss provisions (as happened in 2003) going forward.

As a result of these considerations, staff believes that the SAIF reserve ratio at June 2005 is likely to be unchanged from the current level. Because the entire expected range for the SAIF reserve ratio is greater than the DRR of 1.25 percent, staff believes that it is reasonable to maintain the existing SAIF rate schedule.

Risk-Based Assessment System.

Staff recommends retaining the current spread of 27 bp between the assessments paid by the best- and worst-rated institutions as well as the rate spreads between adjacent cells in the assessment rate matrix. The proposed assessment rate schedule appears in Table 5. The Board previously determined that the current rate spreads provide appropriate incentives for weaker institutions to improve their condition and for all institutions to avoid excessive risk-taking, consistent with the goals of risk-based assessments and existing statutory provisions. The current rate spreads also generally are consistent with the historical variation in institution failure rates across cells of the assessment rate matrix.

Table 5
Proposed Assessment Rate Schedule
First Semiannual Assessment Period of 2005
SAIF-Insured Institutions

Capital Group	A	B	C
1. Well	**0 bp**	**3 bp**	**17 bp**
2. Adequate	**3 bp**	**10 bp**	**24 bp**
3. Under	**10 bp**	**24 bp**	**27 bp**

In setting assessment rates to achieve and maintain the reserve ratio at the target DRR, the Board is required to consider the effects of assessments on members' earnings and capital. The estimated annual revenue from the existing rate schedule is $7 million In recommending that the Board maintain this schedule, the staff has considered the impact on thrift earnings and capital of the current rate schedule and found no unwarranted adverse effects.

The Assessment Base Distribution and Matrix Migration

Table 6 summarizes the current distribution of institutions across the assessment matrix.

Table 6
SAIF Assessment Base Distribution (1)
Assessable Deposits as of June 30, 2004
Supervisory Subgroup and Capital Groups in Effect July 1, 2004

Capital Group		A		B		C	
1. Well	Number	1,082	92.8%	65	5.6%	9	0.8%
	Base ($billion)	$1,081	98.5%	$13	1.2%	$1	0.1%
2. Adequate	Number	7	0.6%	2	0.2%	0	0.0%
	Base ($billion)	$2	0.2%	$0	0.0%	$0	0.0%
3. Under	Number	0	0.0%	0	0.0%	1	0.1%
	Base ($billion)	$0	0.0%	$0	0.0%	$0	0.0%

Estimated annual assessment revenue	$7 million
Assessment Base	$1,098 billion
Average annual assessment rate (bp)	0.06 basis points

Notes:
(1) "Number" reflects the number of SAIF members (excludes BIF-Oakar institutions). "Base" reflects all SAIF-assessable deposits.

With 99.0 percent of the number of institutions and 99.9 percent of the assessment base in the three lowest assessment risk classifications of "1A," "1B," and "2A," as of July 1, 2004, the current distribution in the rate matrix reflects little fundamental difference from the previous semiannual assessment period. The current distribution reflects a slight increase in the percentage of institutions in the best-rated premium category. Since the previous assessment period, 13 institutions migrated into the "1A" risk classification (Table 7), and 14 institutions migrated out of the "1A" risk classification. Only 84 institutions are currently classified outside of the best risk classification.

Table 7
SAIF Migration To and From Assessment Risk Classification "1A"

Institutions entering "1A"	Number	Base ($billion)
Due to capital group reclassification only	0	0.0
Due to supervisory subgroup reclassification only	13	12.7
Due to both	0	0.0
Total	13	12.7
Institutions leaving "1A"	**Number**	**Base ($billion)**
Due to capital group reclassification only	3	0.3
Due to supervisory subgroup reclassification only	11	2.0
Due to both	0	0.0
Total	14	2.3

Notes: The table reflects SAIF-insured institutions that moved in and out of assessment risk classification "1A" from the first semiannual assessment period of 2004 to the second semiannual assessment period of 2004. The numbers only include institutions that were rated in both periods. The table does not reflect other assessment risk classification migrations that are not either to or from "1A."

Overall, the supervisory subgroup component of the risk classification was upgraded since the previous period for 15 institutions with an assessment base of $12.8 billion and was downgraded for 12 institutions with an assessment base of $2.0 billion.

Other Issues

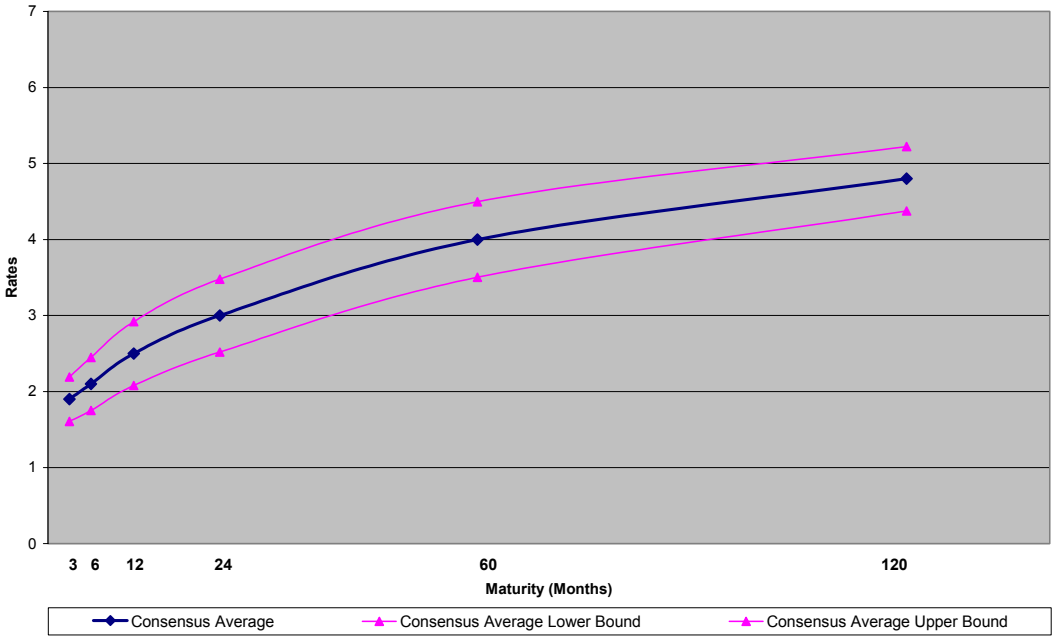
FICO Assessment. The Deposit Insurance Funds Act of 1996 (Funds Act) separates the Financing Corporation (FICO) assessment from the FDIC assessment, so that the amount assessed on individual institutions by the FICO is in addition to the amount paid according to the SAIF rate schedule. All institutions are assessed the same rate by FICO, as provided for in the Funds Act, and the FICO rate is updated quarterly. The FICO rate for the second quarterly payment in the second semiannual assessment period of 2004 will be determined using September 30, 2004 Call Report and Thrift Financial Report data.

STAFF CONTACTS

For information about deposit insurance assessments, please contact Matthew Green, Chief, Fund Analysis Section, Division of Insurance and Research, at (202) 898-3670, or Joe DiNuzzo, Counsel, Legal Division (202) 898-7349. For FICO assessment information, please contact Richard Jones, Chief, Deposit Insurance Pricing Section, Division of Insurance and Research, at (202) 898-6592.

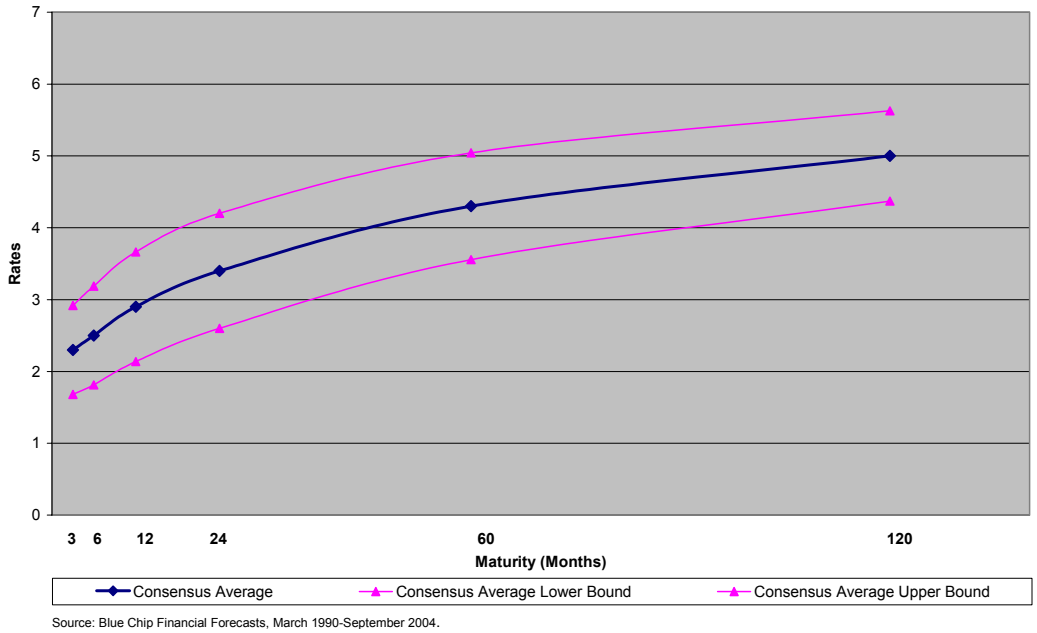
Appendix A – Interest Rate Assumptions

Figure 1: Estimated Yield Curve and Interval for Fourth Quarter 2004



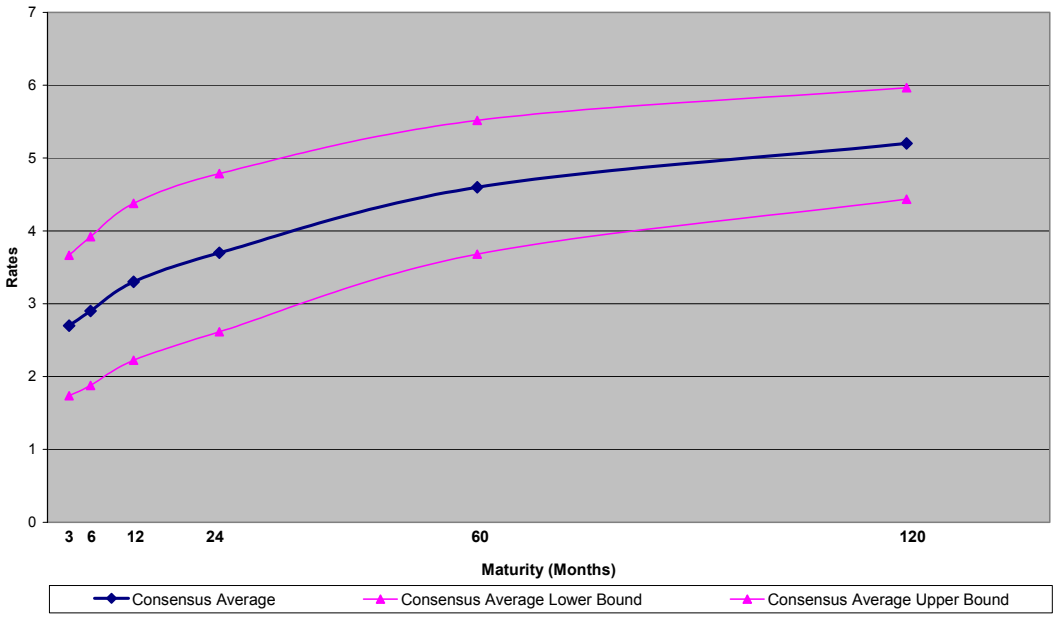
Source: Blue Chip Financial Forecasts, March 1990-September 2004.

Figure 2: Estimated Yield Curve and Interval for First Quarter 2005



Source: Blue Chip Financial Forecasts, March 1990-September 2004.

Figure 3: Estimated Yield Curve and Interval for Second Quarter 2005



Source: Blue Chip Financial Forecasts, March 1990-September 2004.

Concur:

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John M. Brennan
Deputy to the Chairman