

Federal Home Loan Bank of San Francisco
Second Quarter Report
To Our Members

The Bank celebrated a significant milestone in the second quarter of 2000 when advances outstanding surpassed the \$100 billion mark. This achievement once again demonstrates the Bank's support of its members in meeting the credit needs of their communities.

As of June 30, 2000, total advances outstanding reached \$101.2 billion, an increase of \$5.1 billion, or 5%, from March 31, 2000, and \$10.7 billion, or 12%, from December 31, 1999. Total assets grew to \$129.4 billion, increasing \$4.1 billion, or 3%, during the quarter, and \$13.5 billion, or 12%, relative to yearend 1999.

Net interest income for the second quarter was \$132.9 million, an increase of 48% over the year-earlier period. This increase was due to the significant growth in advances, investments, and capital, combined with higher interest rates and spreads.

Net income totaled \$91.4 million for the quarter, an increase of 19% relative to the same period in 1999. The increase in net income was significantly less than the increase in net interest income because the REFCORP assessment is now classified as an expense. Before 2000, the REFCORP assessment was a charge to capital.

The REFCORP assessment for the second quarter was \$22.9 million, reflecting a rate of 20% of net earnings after AHP assessments and operating expenses. The assessment for the second quarter of 1999 was \$11.7 million, reflecting a rate of 15% of net earnings after AHP assessments and operating expenses. After adjusting for the effect of the REFCORP assessment, net income for the second quarter of 1999 was \$65.2 million, and the year-over-year increase in net income was 40%. The increase in the REFCORP assessment accounts for the decline in the Bank's adjusted return on equity for the second quarter from 6.62% in 1999 to 6.35% in 2000. After adjusting for the effect of the REFCORP assessment, the Bank's adjusted return on equity for the second quarter of 1999 was 5.63%.

The Bank paid a quarterly dividend rate of 7.25% (annualized) for the second quarter. The Bank paid out all current period earnings available for dividends, which equaled \$91.4 million, and \$11.5 million of previously restricted retained earnings, which added 0.81% to the annualized dividend yield.

The payout of retained earnings this quarter follows the payout of \$25.4 million of retained earnings in the first quarter. As a result of the passage of the Federal Home

Loan Bank Modernization Act of 1999 and the Federal Housing Finance Board's implementing regulations, the Bank's capital structure will be altered significantly. The Board's decision to pay out retained earnings was based in part on uncertainty about how the expected new capital rules will affect the ownership of the Bank's existing retained earnings.

The Bank had accumulated retained earnings to provide financial flexibility and in anticipation of the possible effect of implementing SFAS No. 133. When SFAS No. 133 becomes effective in January 2001, the Bank expects to recognize the remaining unamortized balance of the deferred losses from certain interest rate exchange agreements terminated by the Bank in 1998. The Bank's Board of Directors decided to retain approximately \$17.1 million in restricted retained earnings to offset the effect of these deferred losses on capital. The full initial impact of SFAS No. 133 on the Bank will not be known until January 2001, and the Bank's retained earnings in the future may not be sufficient to offset the full impact of SFAS No. 133. As a result, the effect of SFAS No. 133 may lead to increased volatility in future dividends.

The Finance Board's proposed rule on "Capital Requirements for Federal Home Loan Banks" was published in the Federal Register on July 13, 2000, and comments are due by October 11, 2000. The proposed capital structure is very different from the stock purchase requirements now in place, and we encourage you to consider how the new capital structure may affect your institution. We are concerned that the November 12, 2000, deadline for the issuance of a final capital rule is impractical given the complexity of the decisions to be made. We hope you will add your voice to ours in encouraging the Finance Board to delay issuance of the final capital rule until the tax, accounting, regulatory and trading/valuation issues implicit in the proposed new capital structure are better understood and a comprehensive analysis of how the proposed new capital structure will work in practice is completed.

Sincerely,



Dean Schultz
President and Chief Executive Officer

Statements of Condition

(In thousands—except par value)	June 30, 2000 (Unaudited)	December 31, 1999	June 30, 1999 (Unaudited)
Assets			
Cash and due from banks	\$ 4,776	\$ 1,424	\$ 1,813
Interest-bearing deposits in banks	1,986,000	1,702,000	1,667,000
Securities purchased under agreements to resell	254,184	2,558,885	1,103,933
Federal funds sold	9,032,000	8,636,000	4,943,000
Investments held to maturity	14,374,424	10,382,029	9,664,161
Advances to members	101,230,338	90,513,829	75,384,115
Accrued interest receivable	2,535,112	2,099,622	1,728,303
Bank premises and equipment, net	4,842	4,324	3,832
Other assets	14,111	13,934	20,397
Total Assets	<u>\$129,435,787</u>	<u>\$115,912,047</u>	<u>\$ 94,516,554</u>
Liabilities and Capital			
Liabilities:			
Consolidated obligations, net:			
Bonds	\$ 84,114,916	\$ 76,725,689	\$ 79,958,739
Discount notes	35,185,649	30,676,746	6,699,517
Total consolidated obligations	<u>119,300,565</u>	<u>107,402,435</u>	<u>86,658,256</u>
Deposits:			
Demand and overnight	247,040	303,143	169,939
Term	22,830	23,810	66,076
Total deposits	<u>269,870</u>	<u>326,953</u>	<u>236,015</u>
Borrowings:			
Securities sold under agreements to repurchase	400,000	—	—
Other	75,000	—	260,000
Total borrowings	<u>475,000</u>	<u>—</u>	<u>260,000</u>
Accrued interest payable	3,351,709	2,606,541	2,425,391
Affordable Housing Program	97,138	90,892	89,633
Payable to REFCORP	22,855	11,184	11,709
Other liabilities	34,100	35,643	149,871
Total Liabilities	<u>123,551,237</u>	<u>110,473,648</u>	<u>89,830,875</u>
Capital:			
Capital stock outstanding (\$100 par value)	5,858,119	5,374,359	4,636,440
Retained earnings:			
Unrestricted retained earnings	29	25,408	10,185
Restricted retained earnings*	26,402	38,632	39,054
Total retained earnings	<u>26,431</u>	<u>64,040</u>	<u>49,239</u>
Total Capital	<u>5,884,550</u>	<u>5,438,399</u>	<u>4,685,679</u>
Total Liabilities and Capital	<u>\$129,435,787</u>	<u>\$115,912,047</u>	<u>\$ 94,516,554</u>

*A portion of restricted retained earnings includes current and prior period income that was restricted in accordance with Federal Housing Finance Board policy. This policy was rescinded on June 22, 2000. The Bank is reviewing the implications of this policy change.

The financial information as of June 30, 2000 and 1999, is unaudited and should be read in conjunction with the audited financial statements for the year ended December 31, 1999, and the accompanying notes thereto. Certain amounts in the 1999 financial statements have been reclassified to conform with the 2000 presentation. The audited financial statements may be obtained by calling 415.616.2610.

Statements of Income

(In thousands)	Three Months Ended		Six Months Ended	
	June 30, 2000 (Unaudited)	June 30, 1999 (Unaudited)	June 30, 2000 (Unaudited)	June 30, 1999 (Unaudited)
Interest Income:				
Advances to members	\$ 1,527,955	\$ 905,060	\$ 2,912,772	\$ 1,727,359
Interest-bearing deposits in banks	22,242	15,475	45,561	25,808
Securities purchased under agreements to resell	22,028	14,726	72,500	44,225
Federal funds sold	129,912	68,203	265,752	146,650
Investments held to maturity	234,925	122,924	395,061	242,470
Loans to other Federal Home Loan Banks	48	230	133	373
Total Interest Income	1,937,110	1,126,618	3,691,779	2,186,885
Interest Expense:				
Consolidated obligations	1,795,129	1,033,265	3,414,223	1,999,441
Deposits	3,111	2,664	6,028	6,512
Securities sold under agreements to repurchase	5,907	502	11,587	1,997
Borrowings from other Federal Home Loan Banks	9	—	9	55
Other borrowings	35	146	64	250
Total Interest Expense	1,804,191	1,036,577	3,431,911	2,008,255
Net Interest Income	132,919	90,041	259,868	178,630
Other Income:				
Prepayment fees, net	50	911	121	948
Services to members	234	180	447	376
Gain on the spin-off/termination involving the Bank's Cash Balance Plan	—	—	—	10,507
Gain on sale of building	—	3,572	—	3,572
Other, net	1,535	744	2,423	2,150
Total Other Income	1,819	5,407	2,991	17,553
Other Expense:				
Operating expense	10,099	9,931	19,783	18,660
Federal Housing Finance Board and Office of Finance expenses	1,457	1,334	2,889	2,720
Total Other Expense	11,556	11,265	22,672	21,380
Income Before Extraordinary Items and Assessments	123,182	84,183	240,187	174,803
REFCORP assessments	22,855	—	44,346	—
Affordable Housing Program assessments	10,158	7,247	19,709	14,983
Total Assessments	33,013	7,247	64,055	14,983
Income Before Extraordinary Items	90,169	76,936	176,132	159,820
Extraordinary gains on early retirement of debt	1,252	—	1,252	—
Net Income	\$ 91,421	\$ 76,936	\$ 177,384	\$ 159,820
Financial Ratios (Annualized)				
	June 30, 2000	June 30, 1999	June 30, 2000	June 30, 1999
Adjusted Return on Equity*	6.35%	6.62%	6.33%	7.05%
Dividend Rate	7.25%	5.24%	7.75%	5.26%

*Adjusted financial performance measures reflect the recognition of advance prepayment fees over the periods remaining through the advances' original maturity dates rather than at the time of prepayment. Extraordinary and other nonrecurring gains and losses are similarly adjusted to provide financial performance measures that are more meaningful when comparing results from other time periods.

The financial information for the periods ended June 30, 2000 and 1999, is unaudited and should be read in conjunction with the audited financial statements for the year ended December 31, 1999, and the accompanying notes thereto. Certain amounts in the 1999 financial statements have been reclassified to conform with the 2000 presentation. The audited financial statements may be obtained by calling 415.616.2610.