



Go Long or Stay Short?

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Member institutions often ask, "Where do you think rates are going?" Of course, if I knew where rates were going, I would be enjoying early retirement on the beach. No one knows where rates are going, but at some point they have to increase.

In this environment, I normally show a barbell approach, keeping some funding short and locking in longer term funding (five years or greater) when the opportunity presents itself. That way you are hedged if rates stay low for awhile or if they begin to trend up. A quick comparison of the one-month advance versus the five-year advance from 1/1/1991-1/27/2010 (nearly 20 years) yields the following results:

	1/1/1991-1/27/2010		1/1/1991-1/27/2010	
	1-Month Advance		5-Year Advance	
Average Rate	4.04%	Date Occurred	5.56%	Date Occurred
Minimum Rate	0.19%	12/24/2009	2.53%	6/13/2003
Maximum Rate	7.60%	1/2/1991	8.46%	6/14/1991
Current Rate	0.24%	1/27/2010	3.01%	1/27/2010

As you can see, the one-month rate averaged 1.52 percentage points lower than the five-year advance average over this time period. The highest one-month rate occurred on 1/2/1991 (7.60 percent) and the highest five-year rate occurred on 6/14/1991 (8.46 percent). The lowest one-month rate occurred on 12/24/2009 (0.19 percent) and the lowest five-year rate occurred on 6/13/2003 (2.53 percent).

Since the one-month rate averaged 1.52 percentage points lower than the five-year advance average, one might assume that it would have been better to stay short over this period as opposed to borrowing some five-year advances. That is both right and wrong. If you had borrowed five-year money below 4.04 percent, you would have done better on average than if you had stayed short. Conversely, if you had borrowed five-year money at more than 4.04 percent, you would have done better sticking with the one-month advance. Currently the five-year advance is 1.03 percentage points below the one-month historical average, so it might be time to explore the opportunity to add some longer-term advances to your funding mix.