# FHLB Des Moines Region Member Meetings

SESSION 4 – ASSET AND FUNDING STRATEGIES

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# Our Series Presenters

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# Making Big Things Happen from Small Actions!
## *2020 FHLB Des Moines Regional Member Meetings*

- Session 1: Managing Your Balance Sheet in Times of Crisis
- Session 2: Creating Your Ideal Funding Plan Structure
- Session 3: Navigating a Flattening Yield Curve During Record Low Rates
- ***Session 4: Asset and Funding Strategies***

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Session 4

# Agenda

1. **Funding Ideas & Issues**
   Deeper dive into Funding Ideas and Issues Today

2. **Segmenting your balance sheet**
   Rethinking the approach and what's working now

3. **Valuing Relationships**
   Evaluating profitability of relationships

4. **What's Next?**

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make big things happen.

# Funding Options Today

Further exploration

# True Statement…

- Any FI funding their entire balance sheet with interest bearing deposits only is paying too much!

- Most efficient cost profile is a blend between retail and wholesale funding
  - The last $1 of retail funding you pay for is always the most expensive $1
  - How much could you lower rates and still hold on to 90-95% of the funds?

- To maximize our "sustainability" we need to optimize our use of all funding sources in a world where deposit preferences have changed over 20-30 years!

# Proof – Marginal Cost Not Average Cost

| Deposit Mix | Balance | Current Cost | | Drop rates | New Balances |
|---|---|---|---|---|---|
| DDA | $ 99.00 | 0.00% | | 0.00% | $ 99.00 |
| NOW | $ 115.50 | 0.15% | | 0.15% | $ 115.50 |
| Savings | $ 132.00 | 0.10% | | 0.10% | $ 132.00 |
| MMDA | $ 165.00 | 1.00% | | 0.90% | $ 156.75 |
| Time - Retail | $ 115.50 | 1.85% | | 1.85% | $ 115.50 |
| Time - Brokered | $ 33.00 | 2.01% | | 2.01% | $ 33.00 |
| **Total Deposits** | **$ 660.00** | **0.72%** | | | **$ 651.75** |
| | Int Exp | 4.755 | | Int Exp | 4.516 |
| | | | | | |
| | Change in Balance | | | $ (8.25) | |
| | Change in Expense | | | $ (0.24) | |
| | ***Cost of the $8.25 million*** | | | ***2.90%*** | |

- Buying the last $8.25 million in MMDA rates by holding rates at 1% vs. 0.90% is effectively paying that money a rate of 2.90%
- What term can you buy for 2.9% today?
  - Retail $
  - Wholesale $

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# Salt Analogy – What Differentiates Deposits?

## Function vs. Perception

## Rate vs. Non-rate Features

### Table salt
Most common
High supply

$0.55 per ounce

### Himalayan pink salt
2nd most common
Medium supply

$0.74 per ounce

### Persian blue salt
Least common
Low supply

$6.28 per ounce

Images

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# Premium Savings – Target Low Balances

## Current Account Rate Sheet

| Account | Balances | Tier | Offer Rate |
|---|---|---|---|
| **Consumer Checking** | **$100,232** | | |
| Regular Checking | $54,388 | | 0.05% |
| Advantage Checking | $19,778 | | |
| Rewards Checking <5k | $4,157 | | 2.05% |
| Rewards Checking >5k | $3,133 | 5,000 | 0.15% |
| Premier Checking | $18,776 | | 0.15% |
| | | | |
| **Consumer Savings** | **$77,762** | | |
| Regular Savings | $48,861 | | 0.05% |
| Passbook Savings | $19,232 | | 0.05% |
| IRA Savings < 15K | $2,321 | | 0.10% |
| IRA Savings > 15K | $7,348 | 15,000 | 0.20% |

- The highest rate offered for a "low balance" consumer is a rewards checking account with an advertised rate of 2.05%.
- But the rewards checking has a high turnover and relatively low balances. Its value is in the fee income and transaction revenue, but it is expensive to replace the turnover.
- Average balances of regular and passbook savings accounts between $500-$5,000 have not been growing, yet they represent 84% of the account holders.

# Premium Savings – Tiered Reward

## New Account Structure

| Tier | Rate | APY at tier |
|---|---|---|
| $0-$500 | 3.00% | 3.03% |
| $500-$1,000 | 0.85% | 1.95% |
| $1,000-$2,000 | 0.60% | 1.27% |
| $2,000-$3,000 | 0.55% | 1.04% |
| $3,000-$4,000 | 0.50% | 0.90% |
| $4,000-$5,000 | 0.45% | 0.82% |
| > $5,000 | 0.40% | APY blends down as balances increase |

- Reduced the thresholds on the rewards account to increase qualification rates.
- Changed pricing rule on rewards rate from best national rate to price in line with best local rewards checking rate – which meant reducing it to 1.85%
- Created a tiered premium savings account as a new account. Requires any existing checking account, supports round-up savings feature. Does not have any other hurdles.
- Targeted average balance goal is $1,500 (compared to typical averages of less than $700).
- Debated a no withdrawal bonus feature, but don't have technology support for that yet. A rate bonus would be added when either consecutive months of equal or higher balances target is met, or with a regular minimum deposit.
- Cost of success was measured with marginal cost model.

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# Premium Savings – Outcomes

## Case 1

- Average balances in (non dormant) accounts between $50-$5,000 did increase.
- In statement savings this was $750. In new account after three months average balances are $1,055.
- More cannibalization than expected from higher balances.
- After three months the premium account represented 4.5% of savings sector balances.

## Case 2

- Different product design, with only one tier. So high rate is only paid on first $2,500.
- Account also has restrictions on initial deposit size  and a maximum monthly deposit of $100.
- Achieving account balance growth rate over 20%, but still only represents 2.5% of total savings balances.
- Considering removing restrictions and adding tiers to also target balances between $10,000 - $20,000.

# Funding Solutions – CDs in Today's Market

- When considering funding costs, we need to set a "horizon"
  - Asset selection
  - Economic conditions
- In this example, under what conditions would it make sense to reach out the yield curve for CD funding?
  - 3 Yr – 3 month spread = 95 bp
  - 5 Yr – 3 month spread = 1.10%

| Term | Ally Bank | FHLB DM | Spread |
|---|---|---|---|
| 3 Mo | 0.50 | 0.40 | 0.10 |
| 6 Mo | 0.75 | 0.42 | 0.32 |
| 1 Yr | 1.50 | 0.57 | 0.93 |
| 3 Yr | 1.55 | 0.74 | 0.86 |
| 5 Yr | 1.60 | 0.97 | 0.63 |

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# Funding Solutions – CDs in today's market

- Let's consider current rates for different products over a 3-year horizon, with the expectation that rates rise 200 bp over 2 years

| | Q1 Start Rate | Q2 | Q3 | Q4 | Q5 | Q6 | Q7 | Q8 | Q9 | Q10 | Q11 | Q12 | 3 Yr Average | 2 Yr Average |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **3 Month** | 0.50 | 0.75 | 1.00 | 1.25 | 1.50 | 1.75 | 2.00 | 2.25 | 2.50 | 2.50 | 2.50 | 2.50 | 1.75 | 1.63 |
| **6 Month** | 0.75 | 0.75 | 1.25 | 1.25 | 1.75 | 1.75 | 2.25 | 2.25 | 2.75 | 2.75 | 2.75 | 2.75 | 1.92 | 1.75 |
| **1 Yr** | 1.50 | 1.50 | 1.50 | 1.50 | 2.50 | 2.50 | 2.50 | 2.50 | 3.50 | 3.50 | 3.50 | 3.50 | 2.50 | 2.25 |
| **3 Yr** | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 | 1.55 |
| **5 Yr** | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 | 1.60 |
| | | | | | | | | | | | | | | |
| **MMDA @ 75% beta and 12 month lag** | 1.10 | 1.10 | 1.10 | 1.29 | 1.48 | 1.66 | 1.85 | 2.04 | 2.23 | 2.41 | 2.60 | 2.60 | 1.79 | 1.59 |

- So what is the all-in cost if rates rise? Is the premium MMDA or higher rate long-term CD a better deal than rolling short-term CDs?
- What if rates ***don't*** rise?
  - CD rates won't rise
  - MMDA Rates could be dropped

**Current FHLB 3 Year Advance = 0.74%**

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# Polling Slide

In today's environment, what products are you offering that will help you grow balances with current and future depositors?

- High rate MMDA or Savings account
- "Rewards" or promotional type checking accounts
- CDs
- All of the above
- I don't know

# Where Do Wholesale Funds Fit?

## Are wholesale funds more than just “bottled water”?

- Advantages
  - Pay an exact price for need funds – no cannibalization
  - Wide variety of providers offering terms and features
  - FHLB offers terms throughout the curve, vs. retail depositors
  - FHLB offers options to manage cost or risk or both!
- Disadvantages
  - Not viewed as a “core funding” component – why?
  - Historical “stigma” over borrowing

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# Blended Funding Revisited

## Example of blended funding – Today's rates

| | | | | |
|---|---|---|---|---|
| | Loan | $200,000 | | |
| Funding Sources | | | | |
| 35% | Core Deposits - Savings Acct | $70,000 | 0.285% | $199.50 |
| 5% | Customer New Deposits | $10,000 | 0.100% | $10.00 |
| 60% | Supplemental Funding FHLB | $120,000 | 1.350% | $1,620.00 |
| 100% | Blended Funding Cost | $200,000 | 0.915% | $1,830 |

Based on estimated duration of loan

## But what about the future cost?

# Blended Funding Revisited – A More Detailed Approach

**Blended Funding Curve Example**

| Term | FHLB Rate | % of FHLB Funding | Cost of Funds | % of COF Funding | Blended COF |
|---|---|---|---|---|---|
| 1 | 0.45% | 0% | 0.05% | 100% | 0.05% |
| 3 | 0.41% | 0% | 0.05% | 100% | 0.05% |
| 6 | 0.43% | 0% | 0.10% | 100% | 0.10% |
| 12 | 0.52% | 0% | 0.50% | 100% | 0.50% |
| 18 | 0.58% | 0% | 0.75% | 100% | 0.75% |
| 24 | 0.60% | 25% | 1.00% | 75% | 0.90% |
| 36 | 0.67% | 25% | 1.20% | 75% | 1.07% |
| 48 | 0.80% | 25% | 1.20% | 75% | 1.10% |
| 60 | 0.93% | 25% | 1.25% | 75% | 1.17% |
| 72 | 1.10% | 30% | 1.25% | 70% | 1.21% |
| 84 | 1.26% | 30% | 1.25% | 70% | 1.25% |
| 96 | 1.47% | 30% | 1.50% | 70% | 1.49% |
| 108 | 1.55% | 30% | 1.50% | 70% | 1.52% |
| 120 | 1.63% | 30% | 1.50% | 70% | 1.54% |
| 180 | 2.01% | 35% | 1.50% | 65% | 1.68% |
| 240 | 2.26% | 35% | 1.50% | 65% | 1.77% |
| 360 | 2.65% | 35% | 1.50% | 65% | 1.90% |

- Ideally, funding costs would be a "curve" that is matched (using FTP) to the cash flows at various points in time.
- In this example, COF are expected in the coming environment
  - Flows through 18 months 100% funded by retail funding costs
  - 18-60 months 75% retail, 25% FHLB
  - 60-1200 months 70% retail, 30% FHLB
  - Etc…
- Using this curve we can assess "deal" profitability using deposit pricing "beta" assumptions

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# Funding Considerations

- Need to have a strong plan focused on product growth, retention and segmentation by demographics, financial factors, channel delivery, etc.

- Set a longer view than where are rates today.
  - Funding is a flow…when it snows on a mountain, the water runs off when the melt-off begins.
  - Daily anomalies can swing FI's away from the plan too easily without discipline and guidelines

- Communicate the plan throughout the institution…knowledge is power!

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# Polling Slide

Is the idea of blended funding” new to you/your FI?

- Yes
- No

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# Moving Back to the Balance Sheet

# What Does Your Balance Sheet Structure Look Like?

- All balance sheets have risk
  - Interest rate risk
  - Credit risk
  - Liquidity risk
  - Regulatory risk
- But do we really consider that risk in the same way when we talk about
  - Investment purchases vs. loan offerings?
  - Borrowing short or long with wholesale vs. buying retail?

# Institution Goals --> Funding Strategy

### Nervous and on Sideline Growing

- 13% capital, feeling smug
- ROA above peer of 0.85%
- Loan growth of 3-5% expected, but worried about continuing – Not chasing deals!
- Loan/Deposits at 68%

We're going to take on all loans we are comfortable underwriting that beat the investment benchmark. Not worried about funding costs.

### Optimistic Grower

- 11.5% capital, just above-board levels
- ROA above target of 1.05%
- Loan growth 3% (if we're lucky)
- Loan/Deposits at 94%

We're going to set ROE targets to maintain earnings and capital. This prices our funding at the margin.

### Aggressive Grower

- 8.2% capital, but RBC is ok
- ROA less important to us than long term ROE
- Loan growth of 10% planned.
- Loan/Deposits at 105%

We're going to compete on price to grow loans. We'll pay whatever we need to fund it.

### Cautious Grower

- 9.6% capital, board a little worried
- ROA of 0.75% below peer
- Loan growth of 6% planned
- Loan/Deposits at 78%

Multiple choices here – depends on priority of growth vs. capital. But earnings are a problem, therefore cost of funds is an issue.

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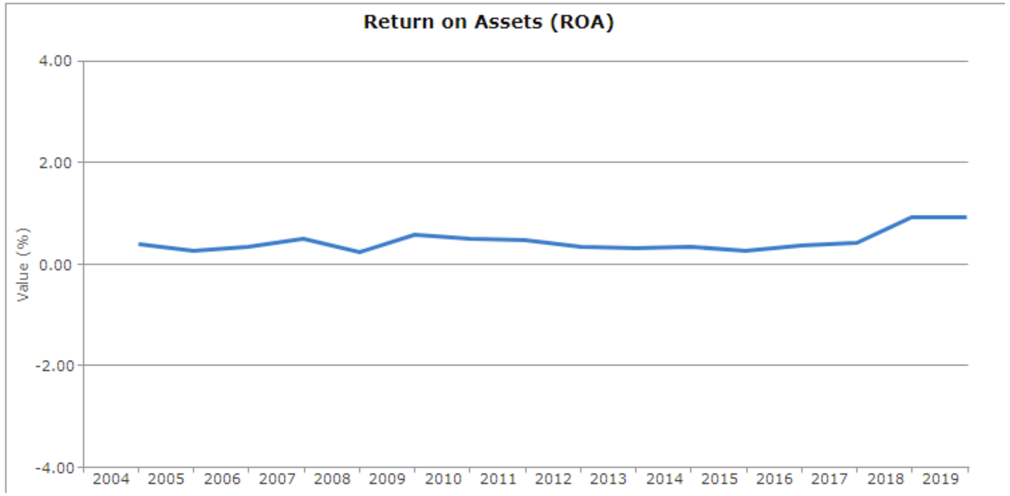
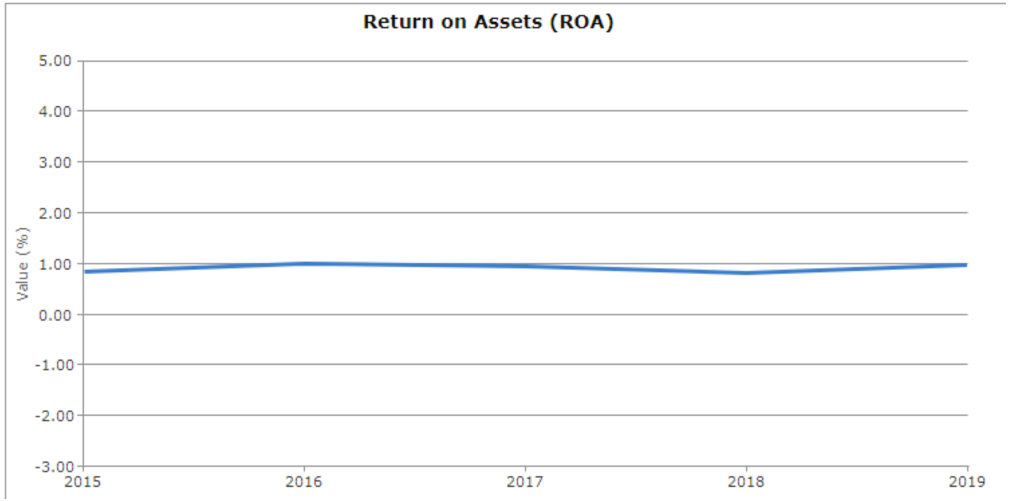
# Polling Slide

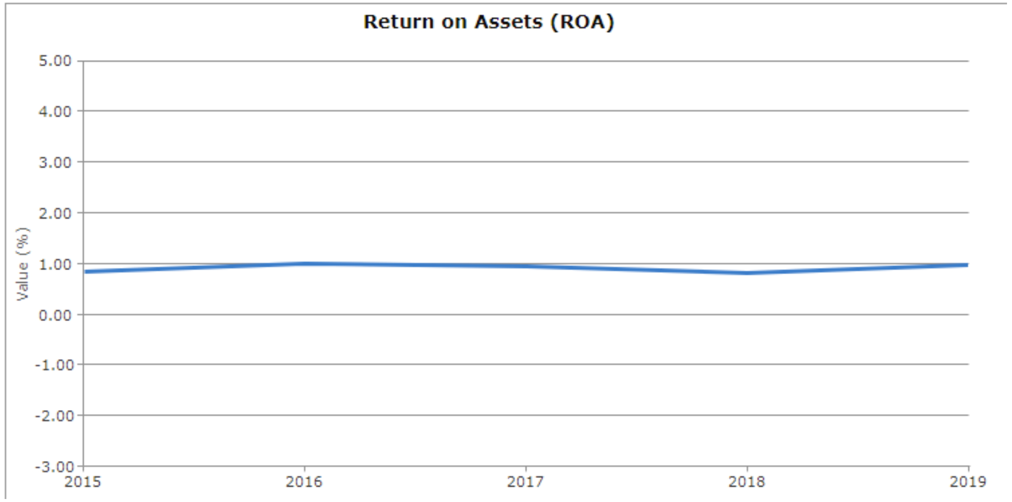
Of the 4 archetypes presented, which one most closely defines your FI?

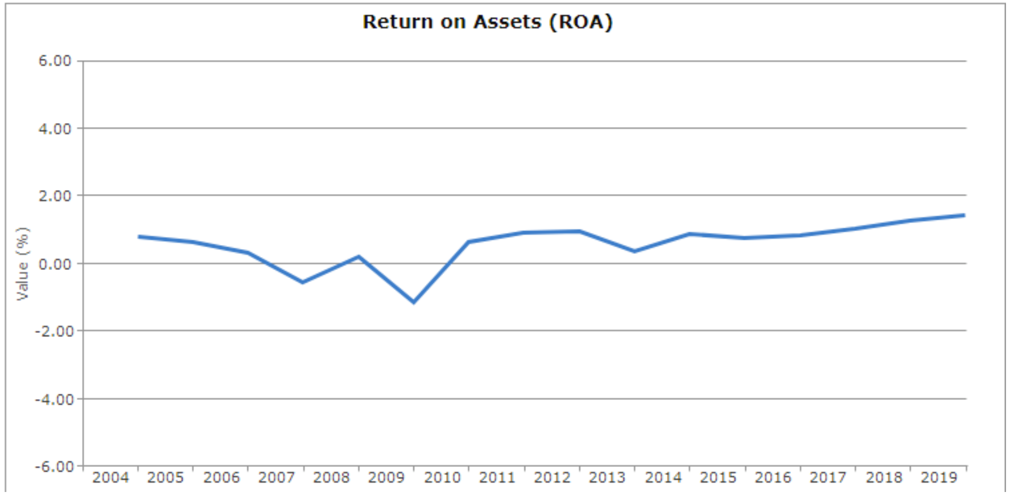
- Nervous and on sideline growing
- Optimistic grower
- Aggressive grower
- Cautious grower

# ROA Comparison – What's the Common Theme?

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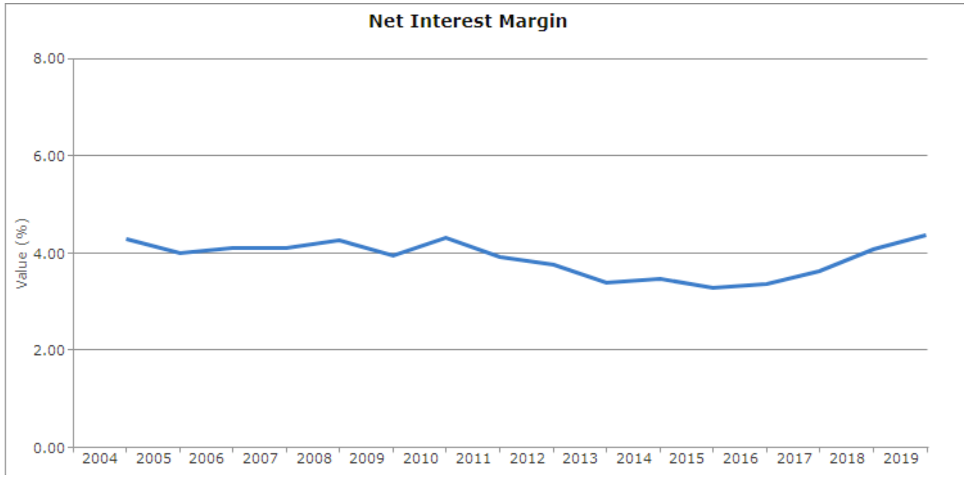
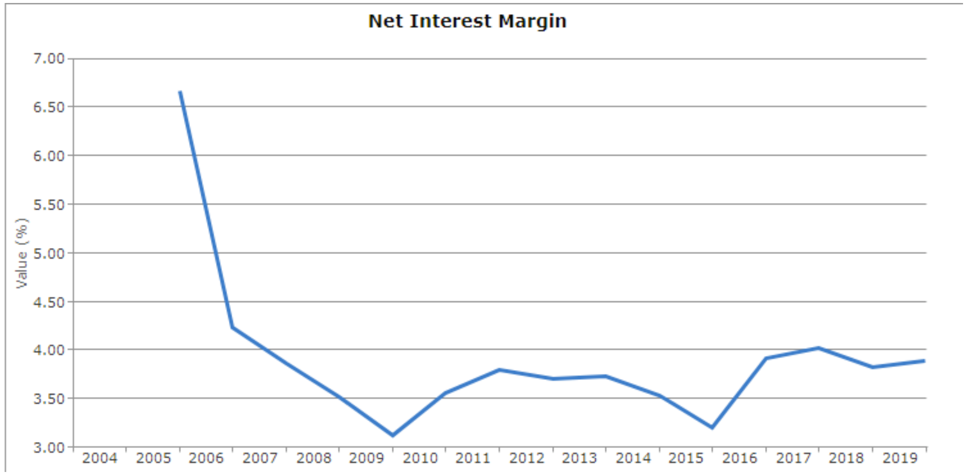
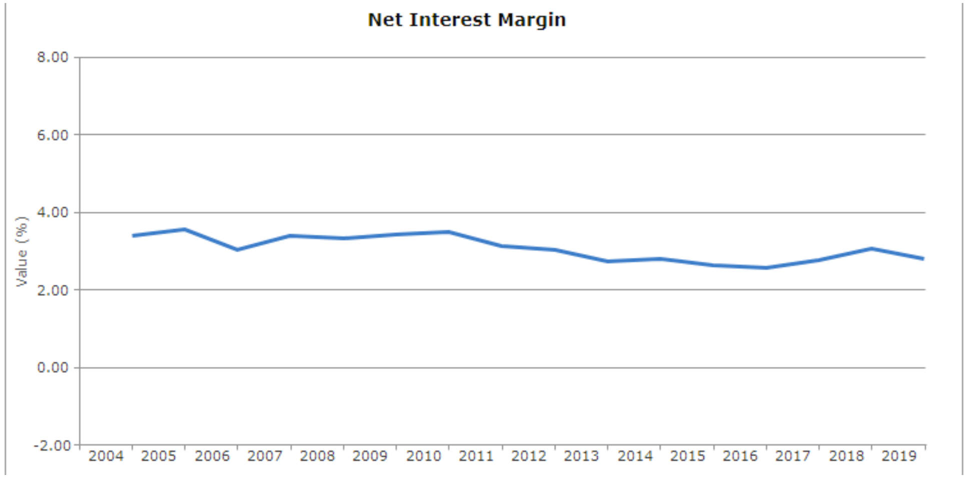
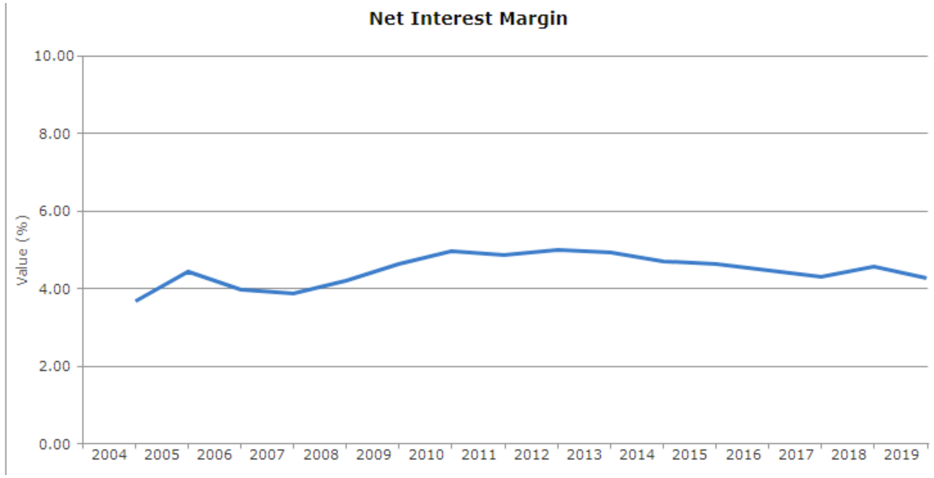
# NII Comparison – What's the Common Theme?

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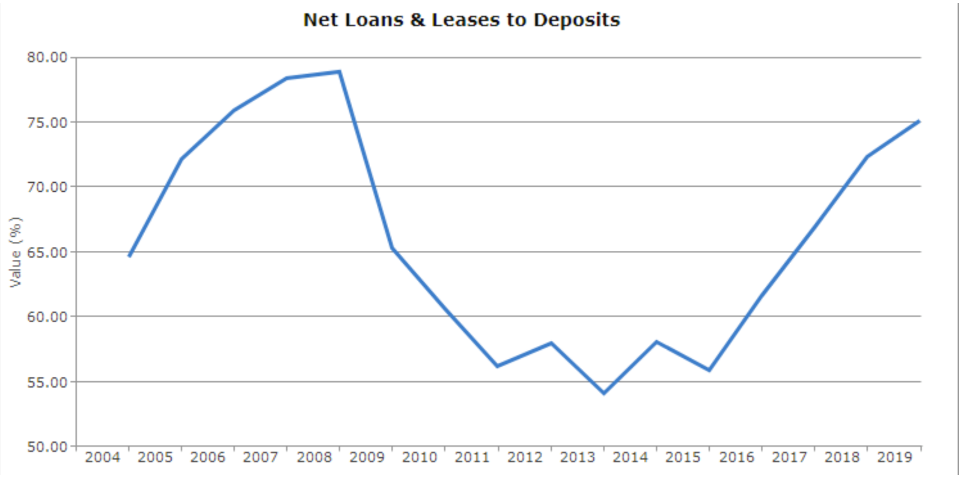
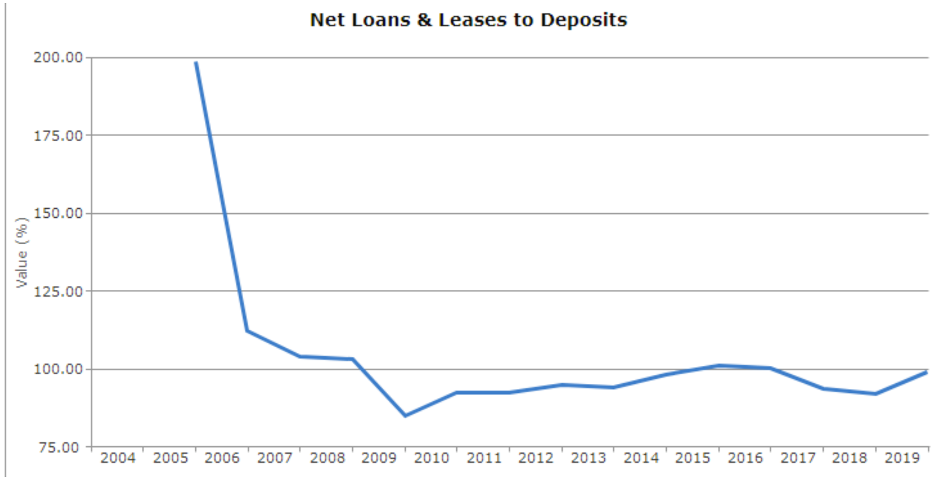
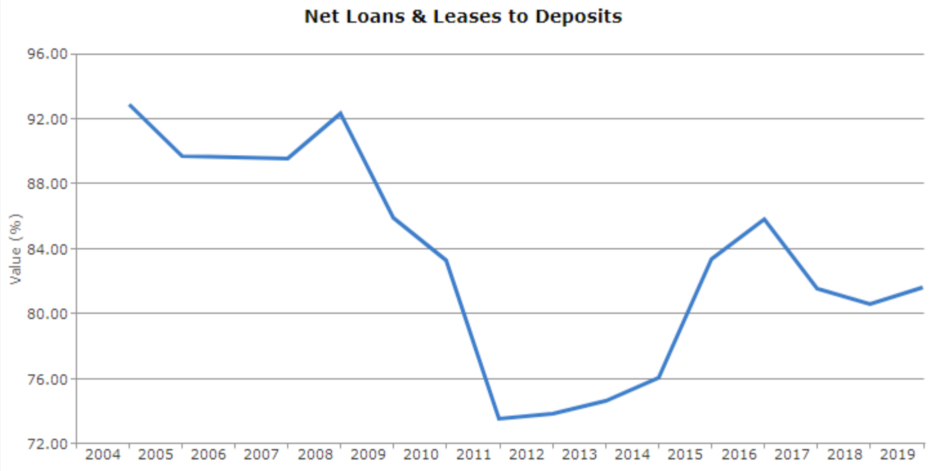
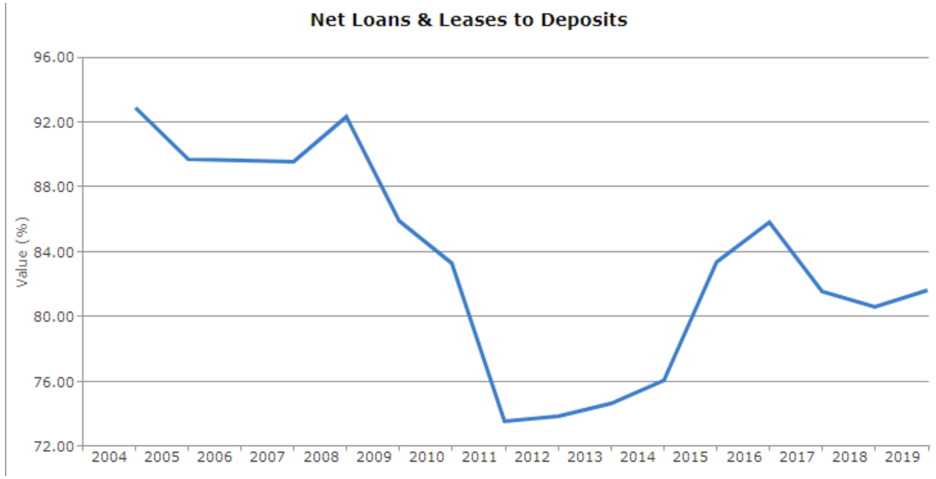
# L/D Ratio Comparison – What's the Common Theme?

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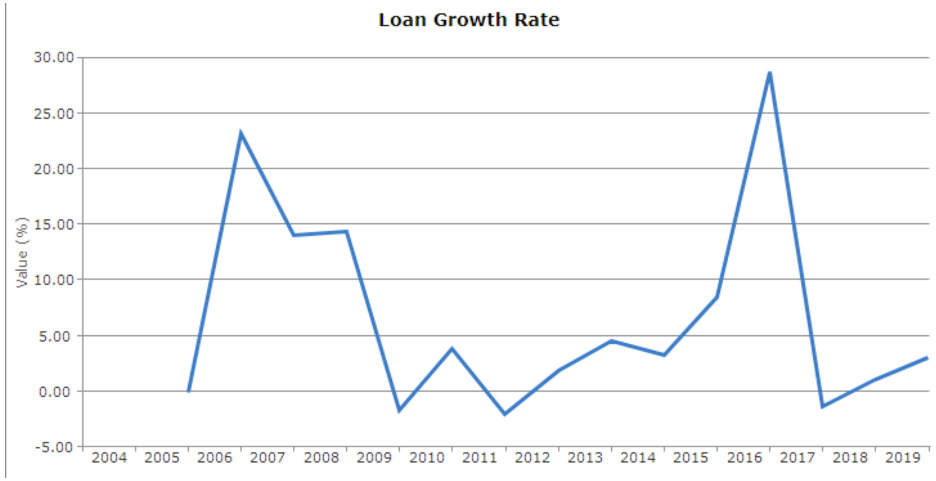
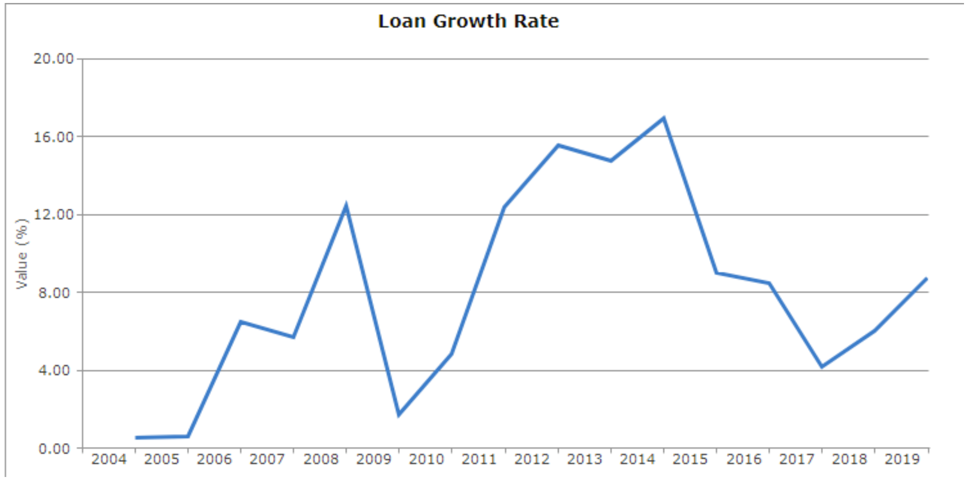
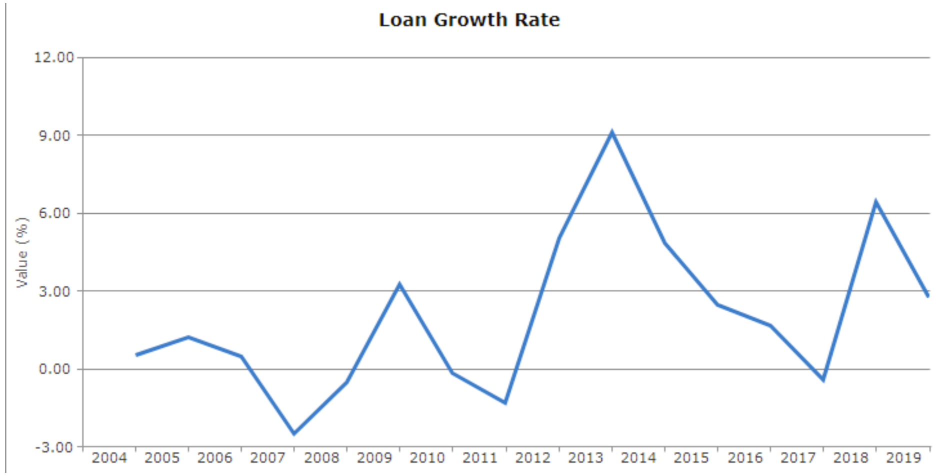
# Loan Growth Comparison – What's the Common Theme?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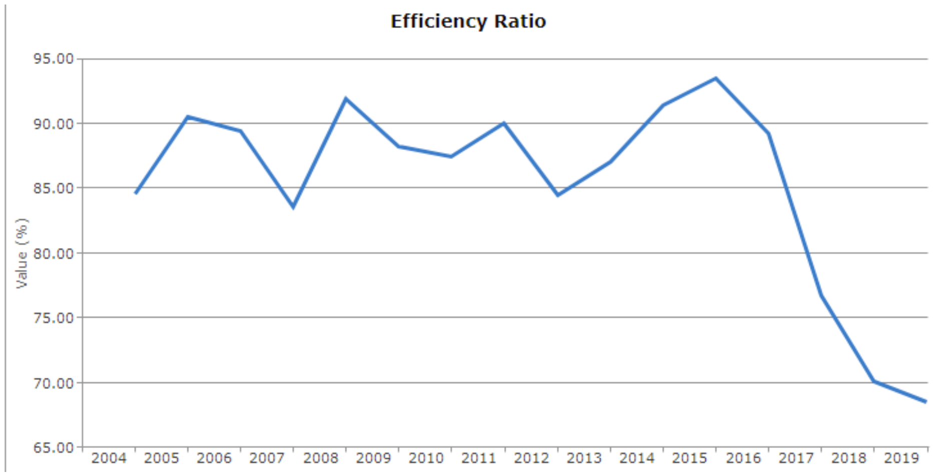
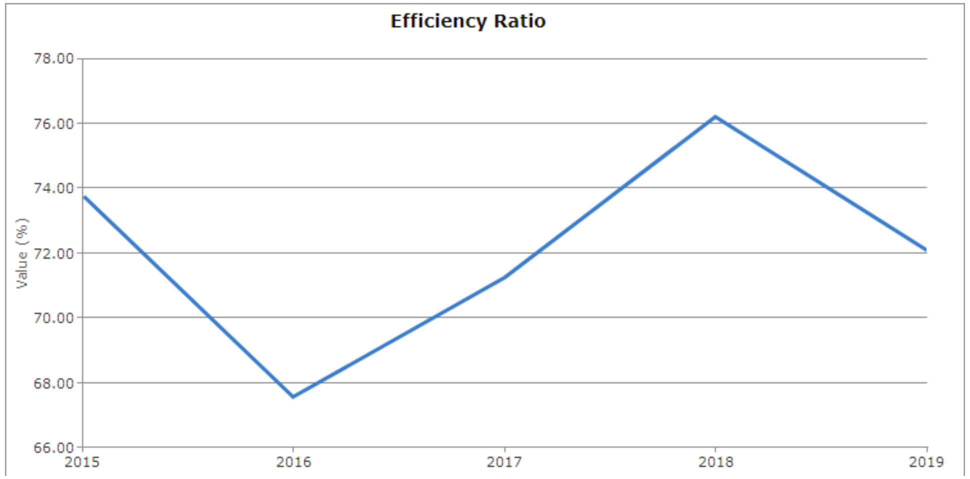
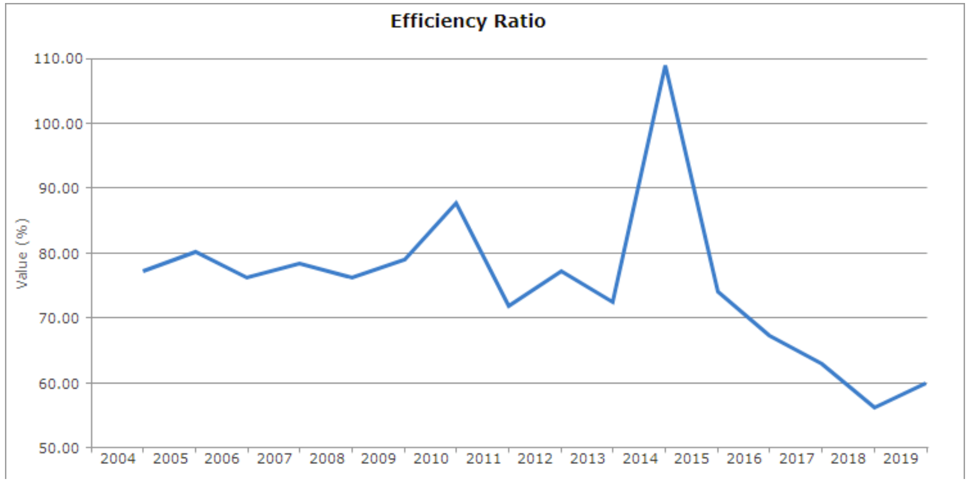
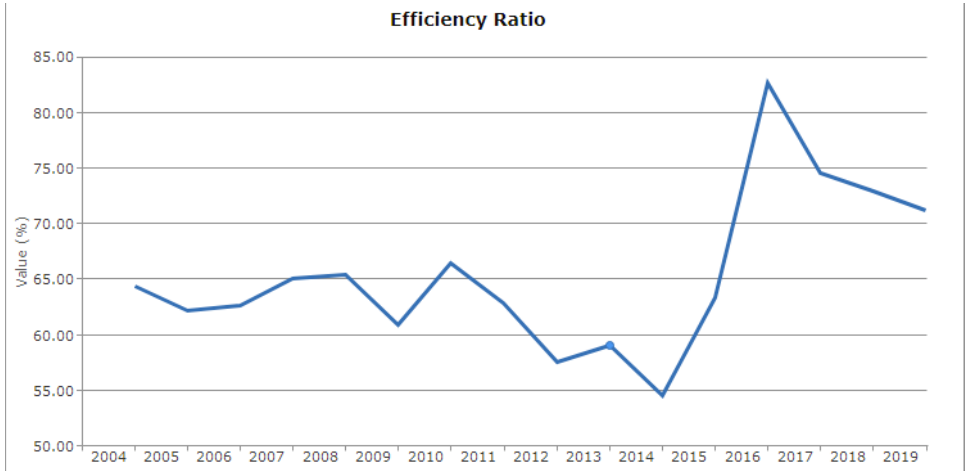
# Efficiency Comparison – What's the Common Theme?

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# Typical Effective Durations for Community FIs

| Asset Class | % of Assets | Effective Durations |
|---|---|---|
| Fed Funds\Cash | 5 - 15% | 1 month |
| Investment Securities | 10 - 15% | 3.5 - 5.2 years |
| Loans | 75 - 85% | 1.75 – 2.5 years |

| Funding Sources | % of Assets | Effective Durations |
|---|---|---|
| DDA | 8 -15% | NA / 10 year+ |
| NOW | 10 – 15% | 3 - 4 years |
| Savings | 14 – 25% | 5 – 10 years |
| Time – Retail | 7 – 15% | 0.5 – 1 year |
| Time Brokered | 3 – 8% | 1.0 – 3 years |

Why do community FI's elect to buy interest rate risk in the investment portfolio while dismissing any consideration in the loan portfolio?

Examples:

- MBS securities
- Municipal bonds
- Loan participations or pools

Does is make sense to use money that we buy from depositors to fund investments with longer durations than loans?

Which option do you have a chance for charging a premium for risk?

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# What Does Your Balance Sheet Structure Look Like?

- What have your asset allocation strategies been for down or flat rate conditions?
  - Our goal:  Increase current earnings by foregoing upside rate movement gains
- Can we segment our own balance sheet into core business and new business?
- Once segmented, can we allocate a portion of assets to carry more risk in order to add return in current and down rates?

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# Reshaping the Current Balance Sheet Position

## Sample Bank Goals:

- Increase current earnings,
- Protect NII in rates down.
- Manage capital to remain "Well Capitalized" with cushion
- Little to no planned asset growth (Pre COVID-19 we expected 5-8%)

## Strategy:

- Reallocate balance sheet to longer duration in order to boost income today and in rates down
    - Shift $100 million in loans to longer duration loans at 4.25%
    - Used blended funding to manage both current cost of funds & beta in rising rates

# Segmented Balance Sheet

Showing dissected balance sheet – core bank (less $100 million) and "Risk Bank"

- Core Balance Sheet

| Income Statement - Core Bank | Rates Down | Rates Same | Rates Up |
|---|---|---|---|
| Int Income / AA | 3.23% | 3.78% | 5.48% |
| Int Expenes / AA | 0.14% | 0.64% | 1.94% |
| NII / AA | 3.09% | 3.14% | 3.54% |
| | | | |
| Non-Int Inc/AA | 1.15% | 1.15% | 1.15% |
| Non-Int Exp/AA | 3.46% | 3.46% | 3.46% |
| Non-Int Margin | -2.31% | -2.31% | -2.31% |
| | | | |
| **Pre-tax, Pre-PLL NI** | **0.78%** | **1.14%** | **1.23%** |
| PLL | 0.20% | 0.20% | 0.20% |
| **NI after PLL** | 0.58% | 0.94% | 1.03% |
| Taxes | 0.20% | 0.32% | 0.35% |
| **ROA** | **0.38%** | **0.62%** | **0.68%** |

- Segmented Balance Sheet

| Income Statement - Risk Bal sheet | Rates Down | Rates Same | Rates Up |
|---|---|---|---|
| Int Income / AA | 4.15% | 4.25% | 4.25% |
| Int Expenes / AA | 0.55% | 1.15% | 1.95% |
| NII / AA | 3.60% | 3.10% | 2.30% |
| | | | |
| Non-Int Inc/AA | 0.00% | 0.00% | 0.00% |
| Non-Int Exp/AA | 0.00% | 0.00% | 0.00% |
| Non-Int Margin | 0.00% | 0.00% | 0.00% |
| | | | |
| **Pre-tax, Pre-PLL NI** | **3.60%** | **3.10%** | **2.30%** |
| PLL | 0.20% | 0.20% | 0.20% |
| **NI after PLL** | 3.40% | 2.90% | 2.10% |
| Taxes | 1.16% | 0.99% | 0.71% |
| **ROA** | **2.24%** | **1.91%** | **1.39%** |

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# Segmented Balance Sheet

- Combined Balance Sheet

| Combined | Rates Down | Rates Same | Rates Up |
|---|---|---|---|
| Int Income / AA | 3.30% | 3.84% | 5.32% |
| Int Expenes / AA | 0.19% | 0.70% | 1.92% |
| NII / AA | 3.11% | 3.15% | 3.40% |
| | | | |
| Non-Int Inc/AA | 1.00% | 1.00% | 1.00% |
| Non-Int Exp/AA | 3.00% | 3.00% | 3.00% |
| Non-Int Margin | -2.00% | -2.00% | -2.00% |
| | | | |
| **Pre-tax, Pre-PLL NI** | **1.11%** | **1.15%** | **1.40%** |
| PLL | 0.20% | 0.20% | 0.20% |
| **NI after PLL** | 0.91% | 0.95% | 1.20% |
| Taxes | 0.31% | 0.32% | 0.41% |
| **ROA** | **0.60%** | **0.63%** | **0.79%** |

- Previous Balance Sheet – No Risk

| Income Statement | Rates Down | Rates Same | Rates Up |
|---|---|---|---|
| Int Income / AA | 2.98% | 3.78% | 5.78% |
| Int Expenes / AA | 0.00% | 0.64% | 2.24% |
| NII / AA | 2.98% | 3.14% | 3.54% |
| | 0 | | 0 |
| Non-Int Inc/AA | 1.00% | 1.00% | 1.00% |
| Non-Int Exp/AA | 3.00% | 3.00% | 3.00% |
| Non-Int Margin | -2.00% | -2.00% | -2.00% |
| | 0 | | 0 |
| **Pre-tax, Pre-PLL NI** | **0.98%** | **1.14%** | **1.54%** |
| PLL | 0.20% | 0.20% | 0.20% |
| **NI after PLL** | 0.78% | 0.94% | 1.34% |
| Taxes | 0.27% | 0.32% | 0.45% |
| **ROA** | **0.52%** | **0.62%** | **0.88%** |

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# Segmented Balance Sheet

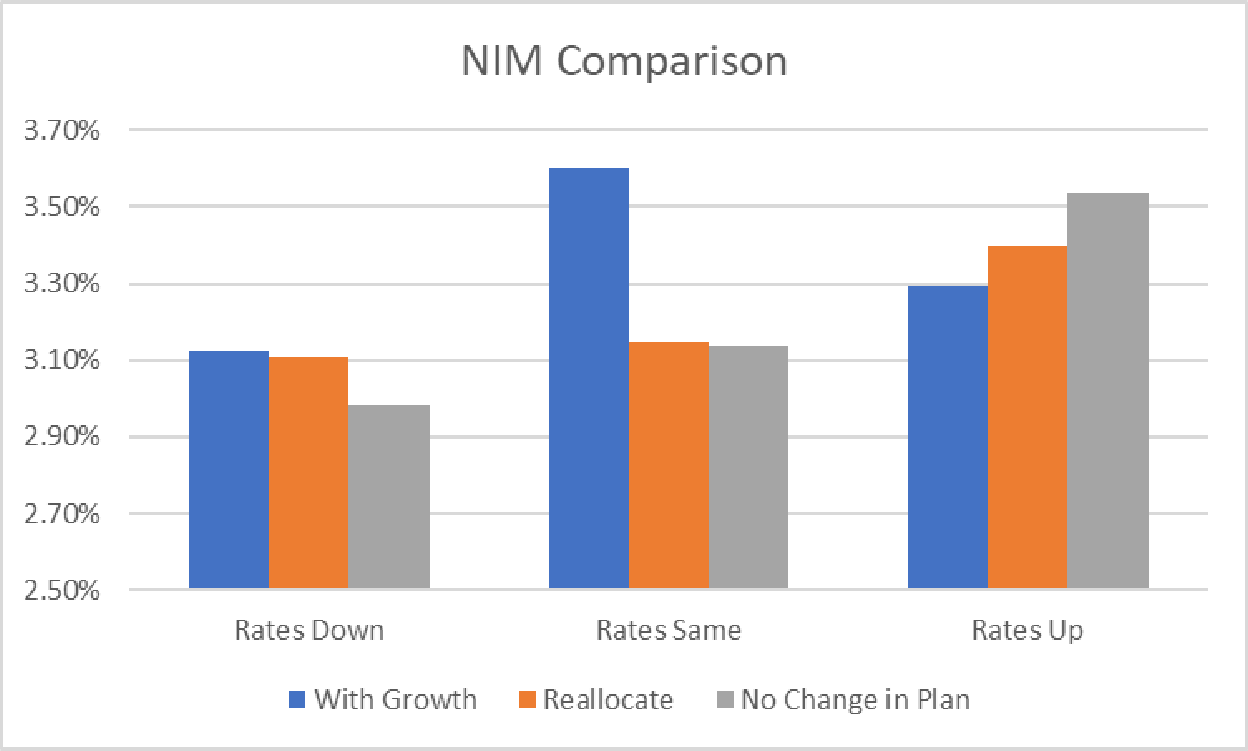
- Combined Balance Sheet

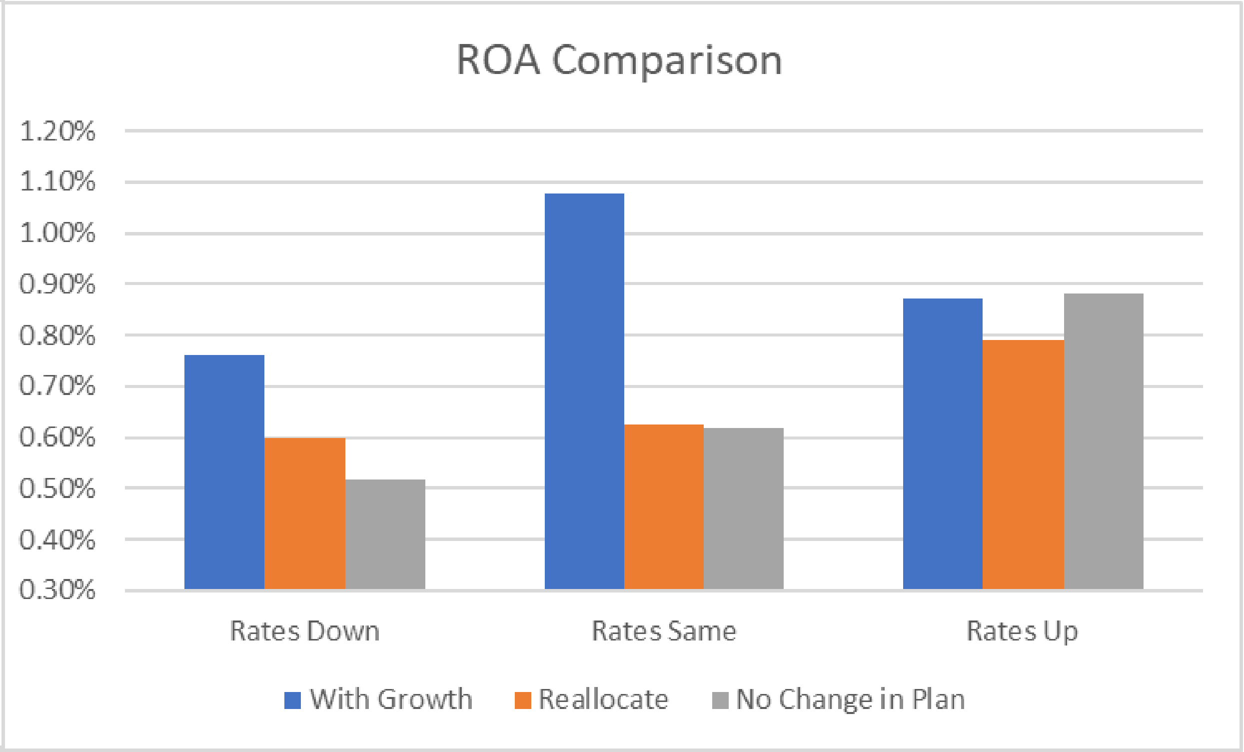
| Combined | Rates Down | Rates Same | Rates Up |
|---|---|---|---|
| Int Income / AA | 3.30% | 3.84% | 5.32% |
| Int Expenes / AA | 0.19% | 0.70% | 1.92% |
| NII / AA | 3.11% | 3.15% | 3.40% |
| | | | |
| Non-Int Inc/AA | 1.00% | 1.00% | 1.00% |
| Non-Int Exp/AA | 3.00% | 3.00% | 3.00% |
| Non-Int Margin | -2.00% | -2.00% | -2.00% |
| | | | |
| **Pre-tax, Pre-PLL NI** | **1.11%** | **1.15%** | **1.40%** |
| PLL | 0.20% | 0.20% | 0.20% |
| **NI after PLL** | 0.91% | 0.95% | 1.20% |
| Taxes | 0.31% | 0.32% | 0.41% |
| **ROA** | **0.60%** | **0.63%** | **0.79%** |

- Additional $100 Million Growth

| Combined | Rates Down | Rates Same | Rates Up |
|---|---|---|---|
| Int Income / AA | 3.35% | 4.34% | 5.19% |
| Int Expenes / AA | 0.23% | 0.74% | 1.90% |
| NII / AA | 3.12% | 3.60% | 3.29% |
| | | | |
| Non-Int Inc/AA | 0.88% | 0.88% | 0.88% |
| Non-Int Exp/AA | 2.65% | 2.65% | 2.65% |
| Non-Int Margin | -1.77% | -1.77% | -1.77% |
| | | | |
| **Pre-tax, Pre-PLL NI** | **1.35%** | **1.83%** | **1.52%** |
| PLL | 0.20% | 0.20% | 0.20% |
| **NI after PLL** | 1.15% | 1.63% | 1.32% |
| Taxes | 0.39% | 0.55% | 0.45% |
| **ROA** | **0.76%** | **1.08%** | **0.87%** |

# Segmented Balance Sheet

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# Relationship Pricing

- Let’s assume you brought in a new borrower (Koch Enterprise) with your PPP loan offering
- Now we want to go after the relationship, what do they have?
  - CRE loan
  - Mortgage Loan
  - Deposit balances
  - Maybe some treasury management fees…
- How do we make this work?

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# Koch Enterprise Opportunity

- Existing PPP Loan
  - 200,000 at 1% with high probability of forgiveness
- New Loan
  - $3 million CRE loan, currently a 5-year balloon/20 Yr Amortization @ 4.125%
  - Looking to refinance to longer term fixed rate
- Your FI is not keen on longer duration, fixed rate loans…
  - How do you keep me?

# Polling Slide

What options would you consider to meet the needs of Koch Enterprise?

- Lower the rate on a 5/20 balloon to avoid long term risk
- Offer a lower rate with point options to “buy down” the rate
- Consider a SWAP transaction to get Koch what he wants and keep the FI in a short-term position
- Offer a long-term, fixed rate loan
- Pass on the deal and/or I don’t know

# Loan Pricing Examples

| | Product | 5/20 Balloon | Fixed 20 Year | Fixed 20 Year |
|---|---|---|---|---|
| **Terms** | Amount: | $200,000 | $200,000 | $200,000 |
| | **Interest Rate %:** | **4.000%** | **4.500%** | **4.3750%** |
| | **Origination Fees%:** | - | - | **0.50 %** |
| **Assumptions** | Origination Exp %: | 1.00 % | 1.00 % | 1.00 % |
| | Annual Servicing %: | 0.75 % | 0.75 % | 0.75 % |
| | Credit Loss Rate %: | 0.45 % | 0.45 % | 0.45 % |
| | **Prepayment %:** | ***10.00 %*** | ***7.50 %*** | **5.00 %** |
| | Tax Rate %: | 36 % | 36 % | 36 % |
| **Results** | Retail Spread: | 2.10 % | 2.29 % | 1.94 % |
| | ROE: | 9.77 % | 10.97 % | 9.30 % |
| | ROA: | 1.95 % | 2.19 % | 2.34 % |
| | Duration: | 3.49 | 6.43 | 7.24 |
| | Price: | 108.45 | 115.57 | 114.61 |

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# Loan Options

- 5/20 priced at 3.50%, no points
- 15 Yr fixed rate priced at 4.125%
- 20 Yr fixed rate priced at 4.375%

- All loans priced using the “blended funding” curve
- All loans use same origination & servicing costs
- Credit risk is assumed to be a 3-rated loan

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# Loan Pricing Example – Blended Funding

| Results | PPP Loan Only | 5/20 Balloon | Fixed 15 Year | Fixed 20 Year |
|---|---|---|---|---|
| Proposed Net Income: | $4,889 | $47,827 | $56,507 | $64,376 |
| Proposed Return on Equity (RAROC): | 28.772% | 15.320% | 18.212% | 20.592% |
| Proposed Return on Assets: | 2.222% | 1.485% | 1.755% | 1.999% |
| Existing Net Income: | $0 | $0 | $0 | $0 |
| Existing Return on Equity (RAROC): | 0.000% | 0.000% | 0.000% | 0.000% |
| Existing Return on Assets: | 0.000% | 0.000% | 0.000% | 0.000% |
| Total Net Income: | $4,889 | $47,827 | $56,507 | $64,376 |
| Total Return on Equity (RAROC): | 28.772% | 15.320% | 18.212% | 20.592% |
| Total Return on Assets: | 2.222% | 1.485% | 1.755% | 1.999% |

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# Loan Pricing Example – Match Fund to Maturity

| Results | PPP Loan Only | 5/20 Balloon | Fixed 15 Year | Fixed 20 Year |
|---|---|---|---|---|
| Proposed Net Income: | $4,889 | $53,613 | $51,580 | $54,294 |
| Proposed Return on Equity (RAROC): | 28.772% | 17.173% | 16.624% | 17.312% |
| Proposed Return on Assets: | 2.222% | 1.665% | 1.602% | 1.660% |
| Existing Net Income: | $0 | $0 | $0 | $0 |
| Existing Return on Equity (RAROC): | 0.000% | 0.000% | 0.000% | 0.000% |
| Existing Return on Assets: | 0.000% | 0.000% | 0.000% | 0.000% |
| Total Net Income: | $4,889 | $53,613 | $51,580 | $54,294 |
| Total Return on Equity (RAROC): | 28.772% | 17.173% | 16.624% | 17.312% |
| Total Return on Assets: | 2.222% | 1.665% | 1.602% | 1.660% |

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# Series Takeaways

- Community FIs must be proactive in managing their "sustainability" by doing what they have done in a new and changing world
  - Offer the products and services to their markets that help the community & FI to grow and thrive
  - Manage risk, but be open to all risks and price the risk
- Funding is the lifeblood of the community FI
  - Develop internal accountability and specific plans to ensure future funding availability
  - Upgrade the reporting and analytical capabilities for assessing the risks and performance
- Asset selection needs to be flexible – meet the needs of the borrower with proper analysis of risk/cost
- Move the ALM process to more proactive discussion of alternative options and less on "regulatory compliance"
- Use your partnerships to help gain the advantages of larger FI's while maintaining the community FI approach
  - FHLB offers liquidity and interest rate risk mitigation solutions so you meet market demand
  - Abrigo brings expertise in advisory services and strong platform products for efficiency

# Polling Slide

How can Abrigo and the FHLB help you moving forward?

- I’d like to be contacted by the FHLB
- I’d like to be contacted by an Abrigo advisor
- I’d like to be contacted by both FHLB and Abrigo
- I’m OK for now

Email specific questions for Abrigo to:
advisory@Abrigo.com

# Thank You

**Program Resource Page**

https://www.abrigo.com/fhlb-des-moines-webinar-series-2020/