FHLBank ATLANTA
A FEDERAL HOME LOAN BANK

MACUMA Annual Leadership Conference
Liquidity Options

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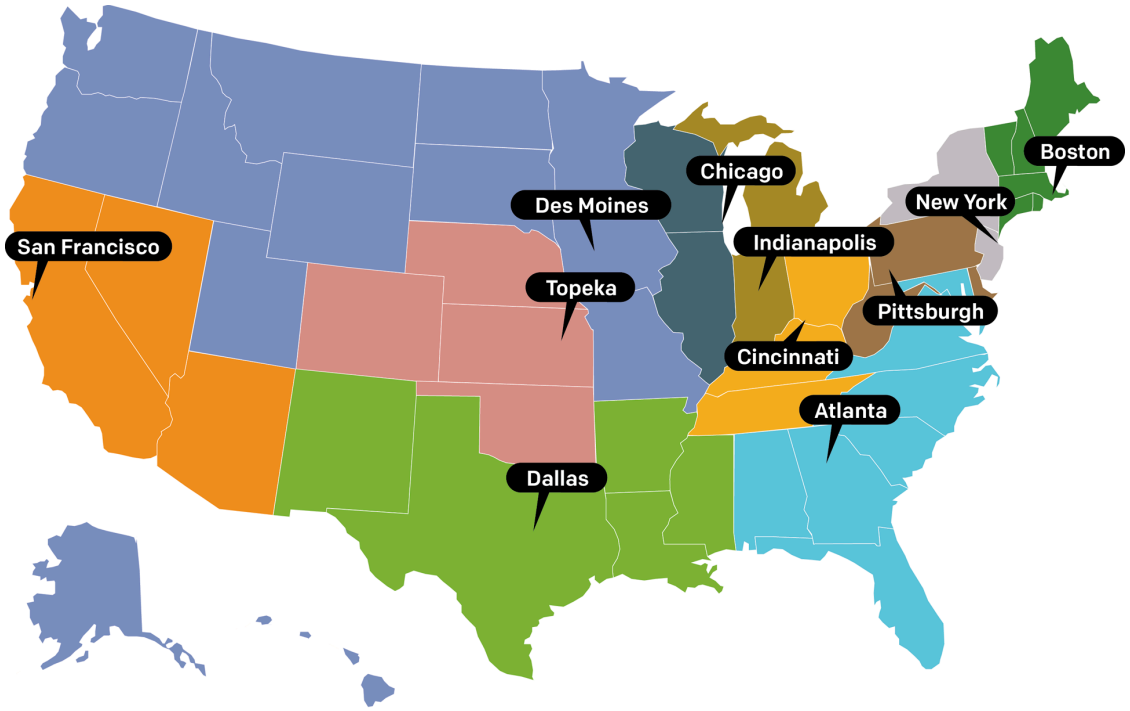
Federal Home Loan Bank Overview



- Cooperatives created by Congress in 1932
- Eleven regional banks with over $1.1 trillion in total assets
- Provide products and services to help roughly 7,000 member financial institutions manage their asset-liability and liquidity programs

What is Liquidity?

The National Credit Union Administration (NCUA) defines liquidity as:

> A credit union's capacity to meet its cash and collateral obligations at a reasonable cost. Maintaining an adequate level of liquidity depends on a credit union's ability to efficiently meet both expected and unexpected cash flows and collateral needs without adversely affecting the credit union's daily operations or financial condition.

Liquidity/asset-liability management is one of the components of the CAMEL rating system and is one of the five critical elements of a credit union's operations that examiners assess in their evaluation of a credit union's performance and risk profile. Ratings are assigned on a 1 to 5 scale with 1 being the strongest.

Liquidity Scenarios

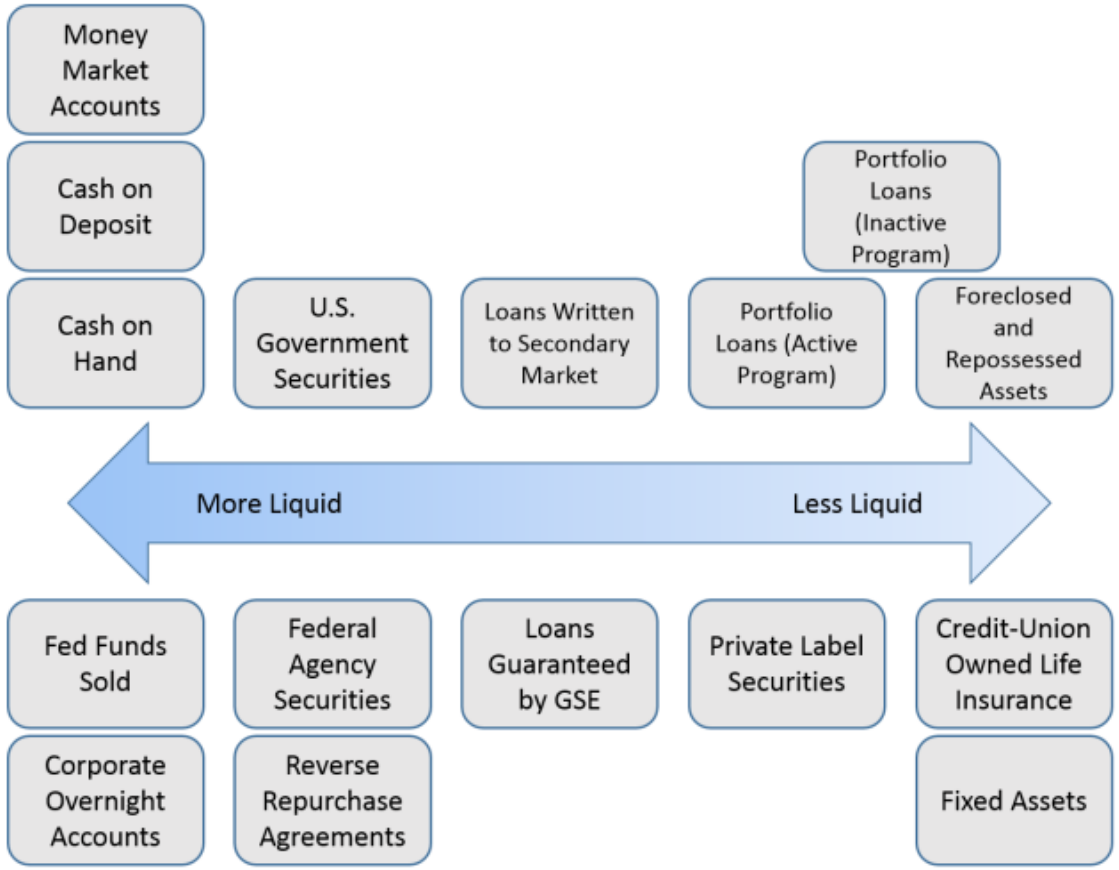
The following table illustrates possible scenarios, depending on a credit union's level of liquidity, per the NCUA's Examiner's Guide:

Inadequate Liquidity	Adequate Liquidity	Excess Liquidity
Credit union is unable to meet member withdrawals, make loans, and/or pay expenses. Any of these scenarios can lead to a disruption in a credit union's operations, decline in member base, and threaten a credit union's solvency.	Credit union has adequate cash or liquid assets on hand to meet current obligations, and has a liquidity cushion available to meet unexpected demands for cash without incurring unacceptable losses.	Credit union is missing opportunities to put excess funds to use (for example, by making loans or purchasing investments) and losing out on potential income.

- To maintain adequate liquidity, a credit union should estimate and plan for liquidity demands over various periods, and consider how funding requirements may change under various scenarios
- Liquidity management is an ongoing responsibility of a credit union's board of directors and management (and ALCO, when appropriate)

Sources of Liquidity: Asset-Based Liquidity

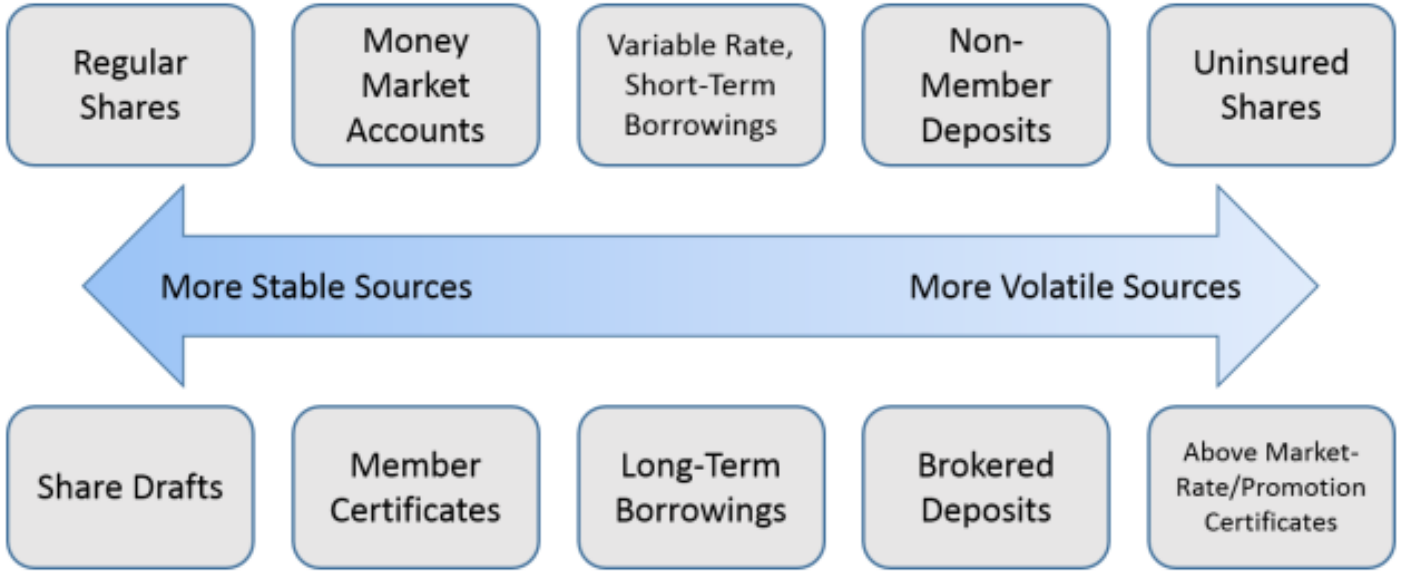
Asset-based liquidity sources include cash, loans, and investments



Source: NCUA Examiner's Guide

Sources of Liquidity: Liability-Based Liquidity

Liability-based liquidity refers to funding available from sources such as member shares, nonmember deposits, uninsured shares, and borrowings



Source: NCUA Examiner's Guide

Sources of Liquidity: Asset-Based Cash Flow

Credit unions may generate cash flows from normal operations and ongoing business activities. Operating income can be a source of funds that bolsters liquidity.

- **Loan income** includes any interest on loans to members; this source of funding can be affected by changes in interest rates and prepayment speeds
- **Investment income** includes any interest or dividends earned on investments a credit union owns; this source of funding can be affected by changes in interest rates
- **Fee income** includes fees charged to members for services (for example, overdraft fees, ATM fees, credit card fees)

Source: NCUA Examiner's Guide

Sources of Liquidity: Contingent Federal Liquidity Providers

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- The third line of protection (after on-balance-sheet liquidity and access to market sources of funds) is access to a contingent federal liquidity provider such as the Federal Reserve Discount Window or Central Liquidity Facility (CLF)
- The Discount Window and CLF exist to provide backup liquidity in circumstances where on-balance-sheet liquidity and market funding sources prove inadequate. While sparingly used, the Discount Window and CLF have proven to be dependable sources of liquidity in times of crisis or unexpected events
- Credit unions under $250 million in total assets are not required to establish access to a contingent federal liquidity source. However, NCUA encourages all credit unions to do so if their contingency funding analysis identifies liquidity events that pose a real threat to the credit union
- The discount window is designed to handle ***sudden*** emergencies or operational issues that require same-day access to contingent federal liquidity
- The CLF is designed to handle ***sustained*** emergencies or operational issues that require contingent federal liquidity for a few days up to several months

Source: NCUA

Liquidity: Cash Flows

- **Forecast Cash Flows**
  - Cash flow projections can help plan for liquidity needs and help make decisions with regard to liquidity excesses or shortfalls
- **Assumptions**
  - Should be reasonable and supportable, management should conduct back-testing by comparing projections to actual results and make adjustments as appropriate
- **Stress Testing**
  - Can help credit unions prepare for unplanned adverse scenarios. The tests and their outcomes are used to identify and quantify sources of potential liquidity strain and the impact on the liquidity position

Source: NCUA Examiner's Guide

Liquidity Risk Management: People

People involved in overseeing and executing liquidity risk management include:

- **Board of Directors** – Ultimately responsible for the liquidity risk assumed. The board's risk management policies should address liquidity and contingency funding needs
- **Management** – Overseeing the development and implementation of appropriate risk measurement and reporting systems, a contingency funding plan, and an effective system of controls over liquidity management
- **ALCO** – Board may appoint an Asset/Liability committee to monitor the liquidity profile. The committee should ensure the risk measurement system adequately identifies and quantifies risk exposure and that the reporting process communicates accurate, timely, and relevant information about the level and sources of risk

Source: NCUA Examiner's Guide

NCUA Rules and Regulation Part 741.12: Liquidity and Contingency Funding Plans

It is essential for every credit union to have a sound process for identifying, measuring, monitoring, and controlling liquidity risk that is commensurate with each credit union's needs

Effective March 31, 2014 as follows:

- **Credit Unions Less than $50 Million in Total Assets Must Have:**
  - a written Liquidity Policy that provides a framework for managing liquidity
  - a list of contingent liquidity sources
- **Credit Unions >$50 Million but less than $250 Million in Total Assets Must Have:**
  - a written Liquidity Policy that provides a framework for managing liquidity
  - a Contingency Funding Plan (CFP)
- **Credit Union >$250 Million in Total Assets Must Have:**
  - a written Liquidity Policy that provides a framework for managing liquidity
  - a Contingency Funding Plan (CFP)
  - access to at least one contingent federal liquidity source

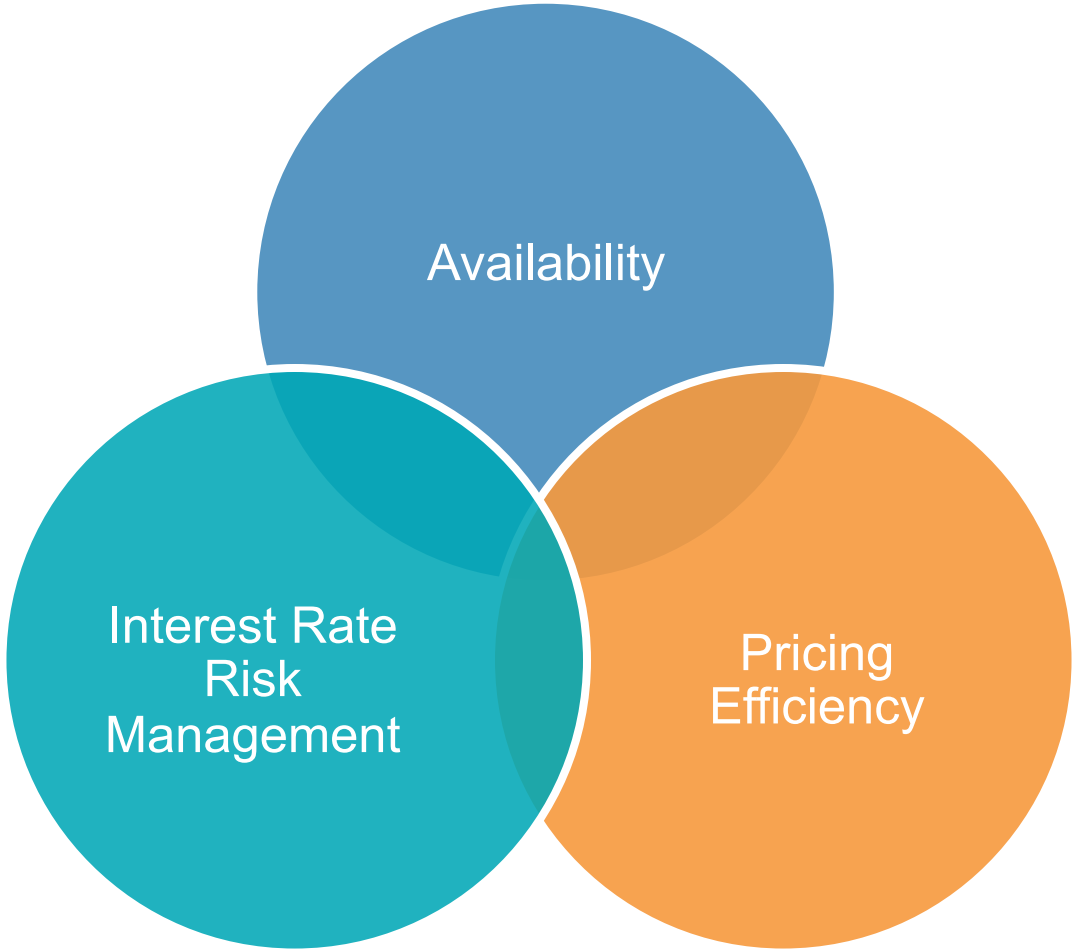
NCUA Rules and Regulation Part 741.12: Contingency Funding Plan Specifics

A CFP includes policies, procedures, projection reports, and action plans designed to ensure your credit union's sources of liquidity are sufficient to fund operating requirements under contingent liquidity events. Per the NCUA, a CFP needs to:

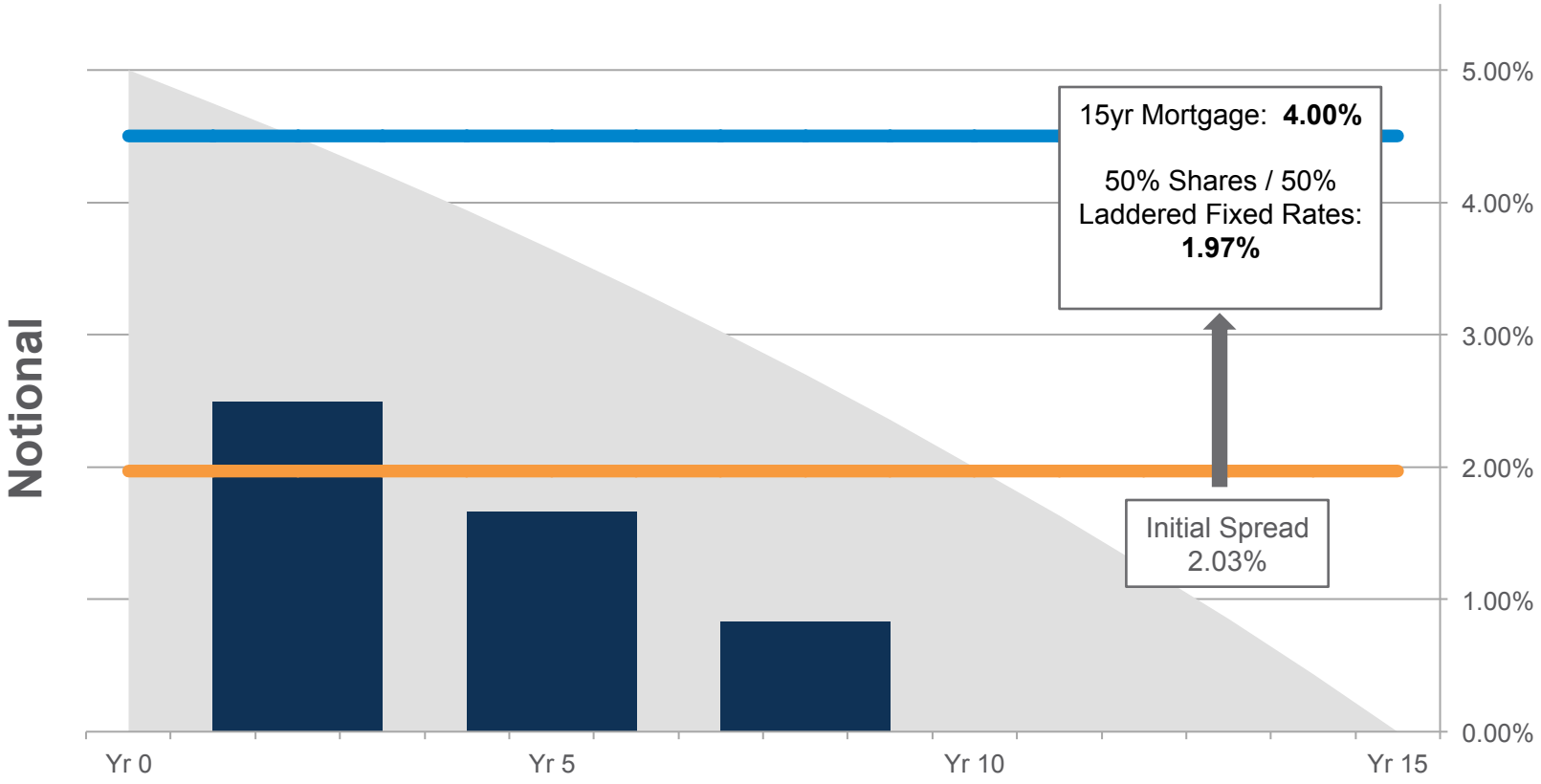
- Specify the frequency the plan will be tested and make necessary updates
- Include a process to forecast and assess liquidity
- Identify specific contingency sources
- Specify how the credit union will manage a range of liquidity-stress events
- Identify lines of authority for managing liquidity events
- Outline the management processes to follow when responding to liquidity events

WHAT SHOULD A CFP ADDRESS?

Creating A Non-Core Funding Strategy



Blended Laddered Funding Strategy Example: 15-year Mortgage for Portfolio



- 50% Shares at 0.75%
- 50% Fixed rate ladder of 3yr (3.04%), 5yr (3.15%), 7yr (3.35%)

Pricing as of 9/17/2018

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