



Liquidity Risk & Funds Management

New York Region Regulatory Teleconference

September 30, 2014

Scope of Discussion

- **Liquidity Trends**
- **Measurement Systems**
- **Stress Testing Practices**
- **Contingency Funding Plans**
- **Ripple Effect of Interest Rate Risk**
- **Q&A Open Forum**

Liquidity Evolution: Then & Now

1995

Asset-Based Liquidity Management

Static Balance Sheet Ratios (Liquidity Ratio)

Securities Assumed Liquid & Loans Considered Illiquid

Wholesale Lines & Pledging Limited

2014

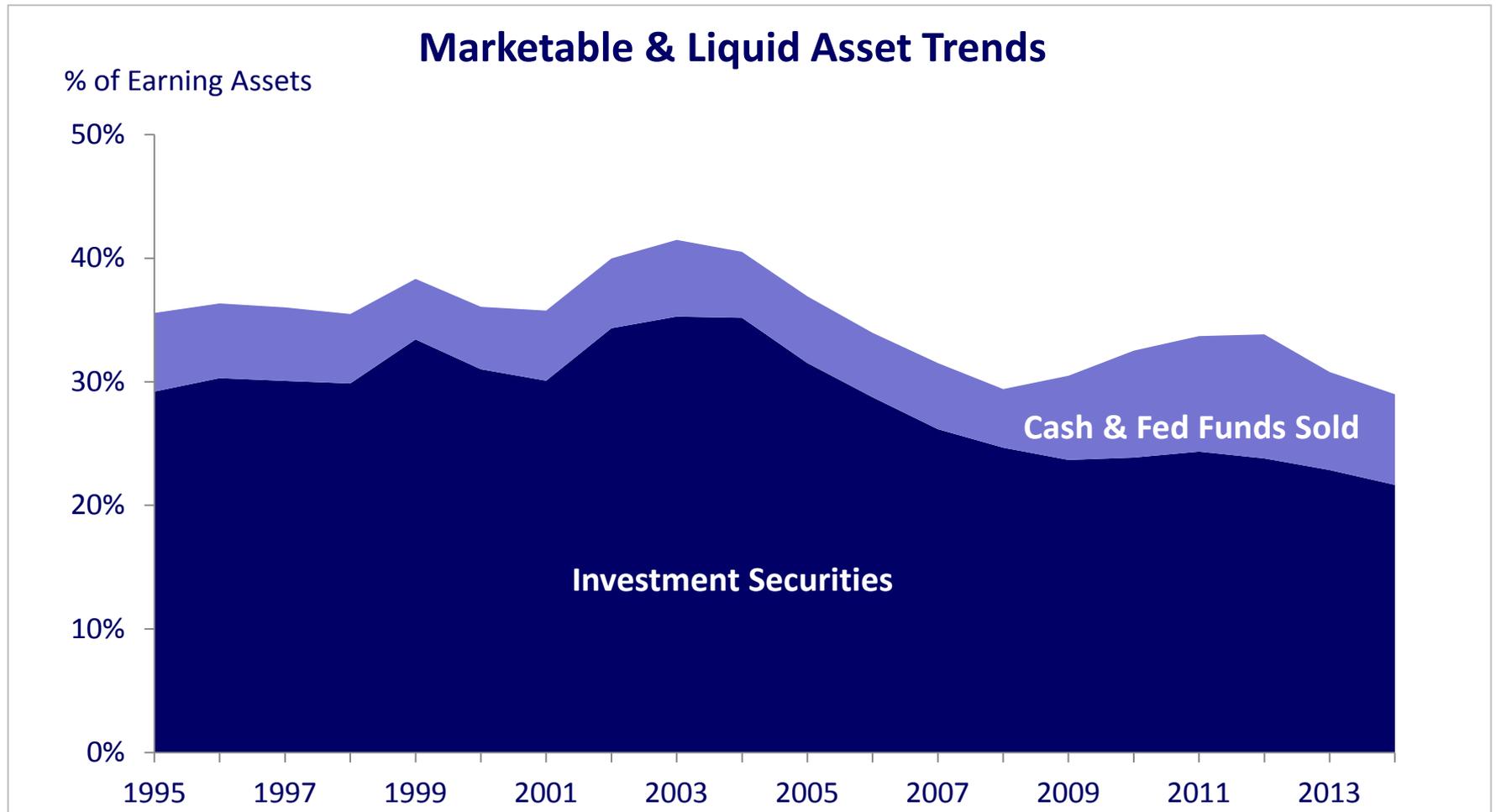
Balanced Funds Management Approach

Forward-Looking Cash Flow Analysis & Stress Testing

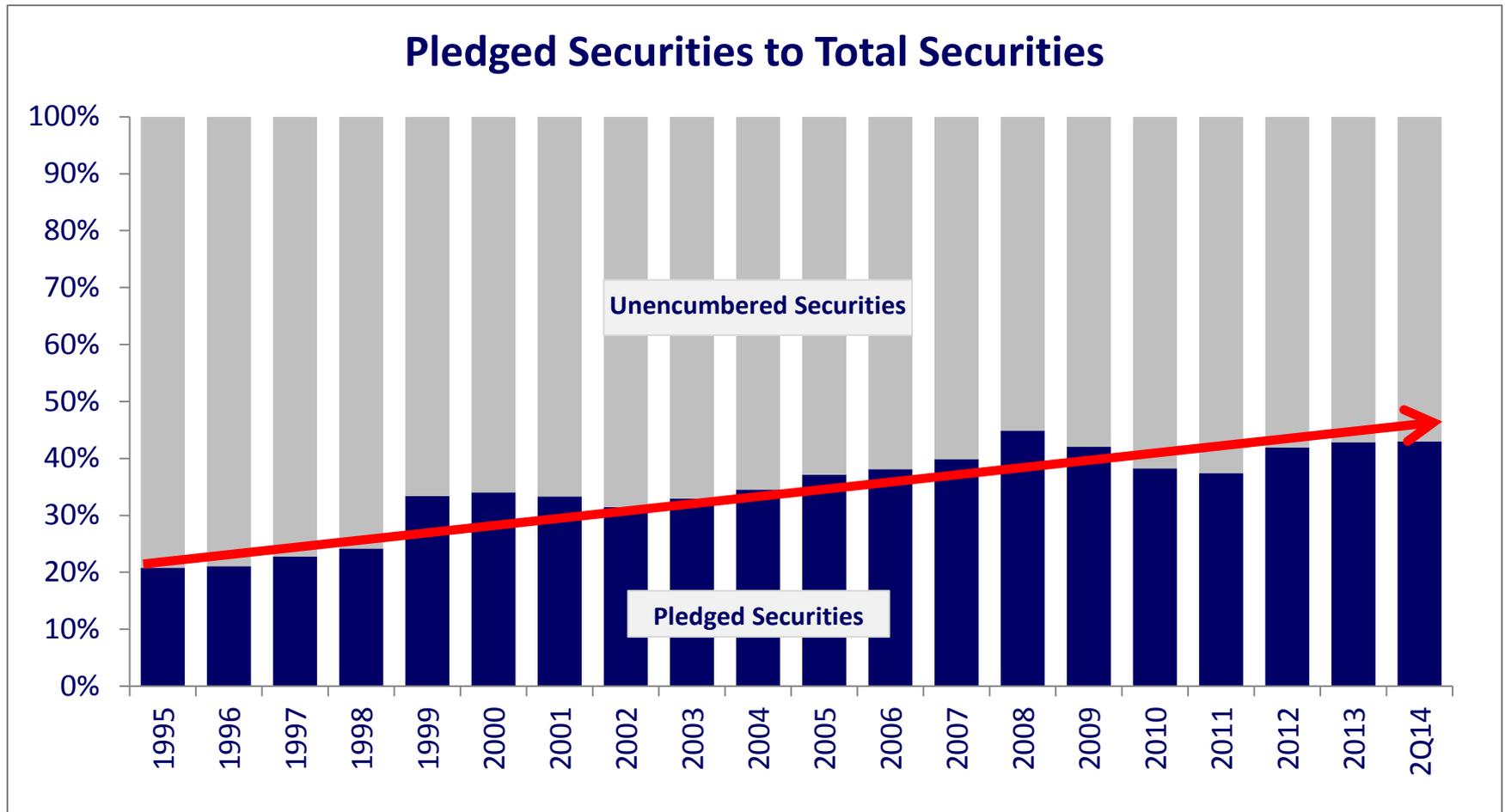
Less Liquid Securities & More Saleable Loans

Wholesale Lines & Pledging Expanded

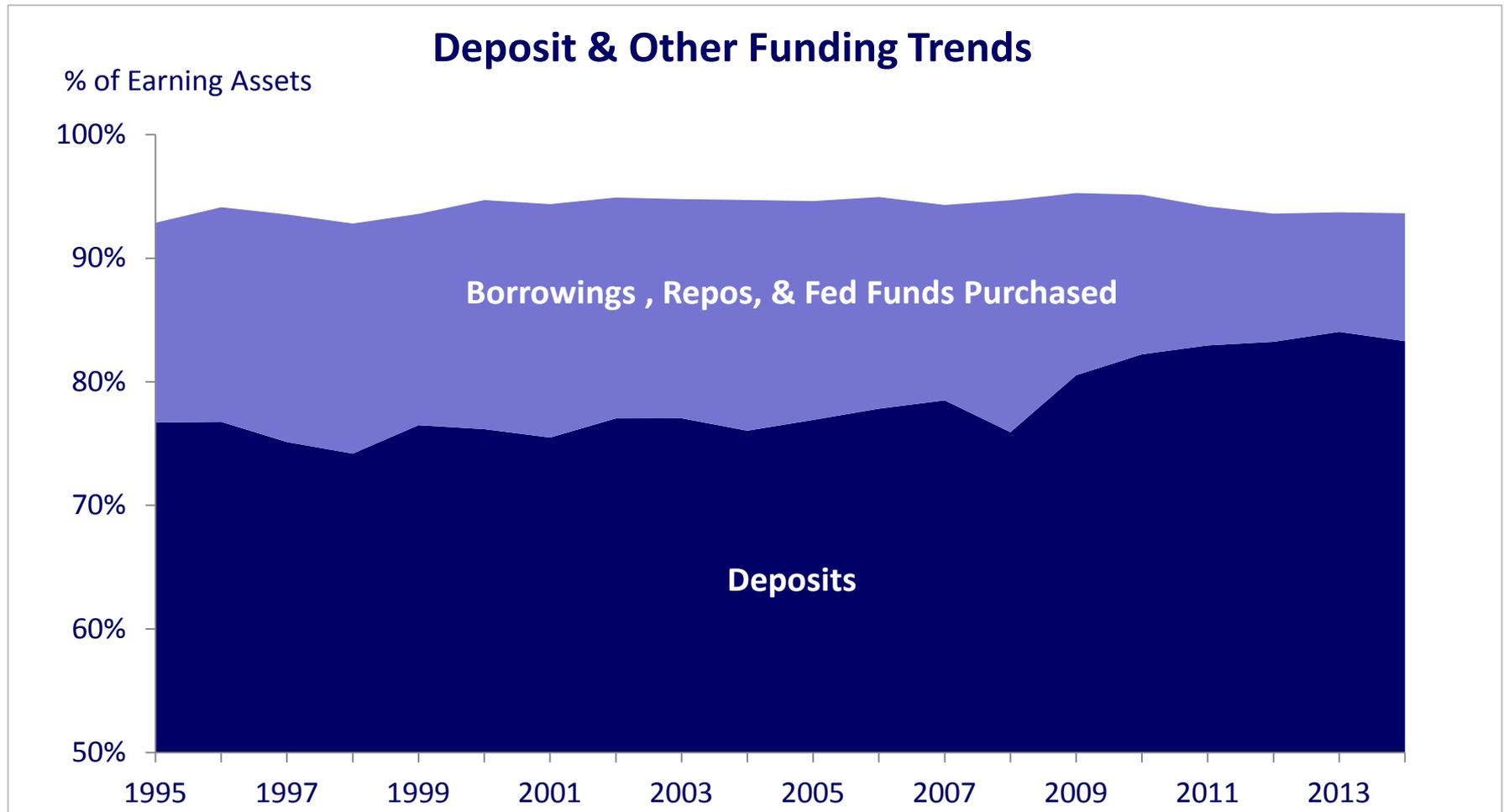
Industry Trends – Asset Based Liquidity



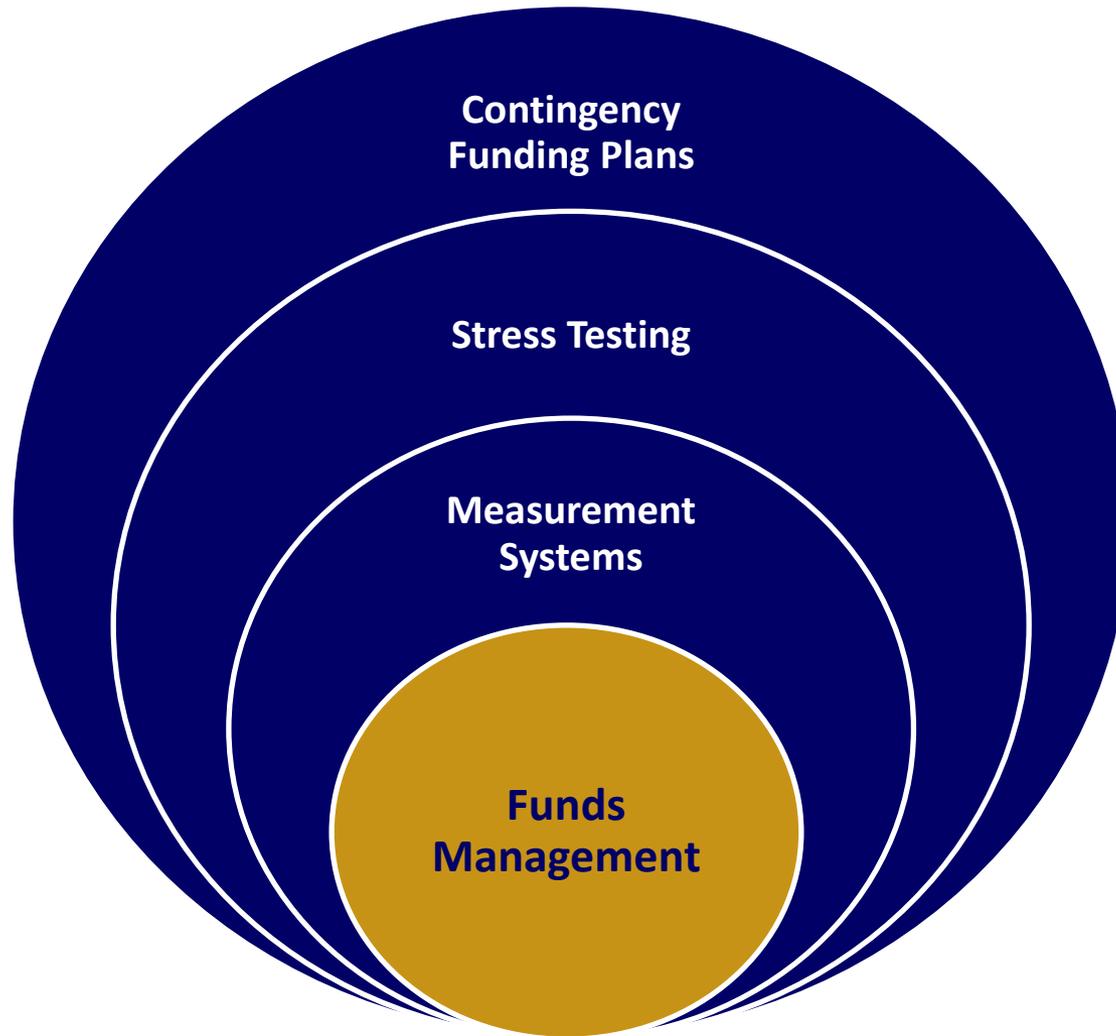
Industry Trends - Pledged Securities



Industry Trends – Liability Based Funding



Funds Management



Measurement Systems – Expectations

- **Pro Forma Cash Flow Projections**
 - Varying Time Horizons
 - Categories of Sources & Uses
 - CASH – Outflows + Inflows

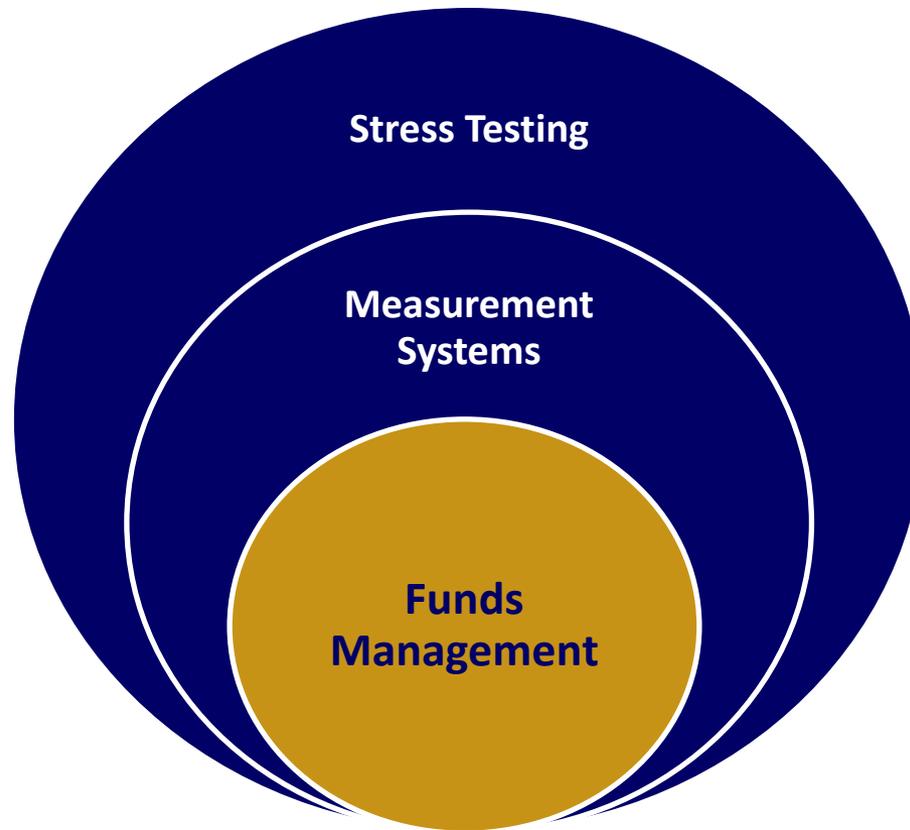
- **Other Liquidity Measures**

- **Documented & Supported Assumptions**

Measurement Systems – Best Practices

- **Additional Liquidity Measures**
 - Customized (Bank-Specific) Ratios
 - Forward Looking Measures & Funding Analytics
- **Robust Time Horizons**
 - Immediate-Term (Daily) Assessments
 - Longer-Terms for Potential Liquidity Events
- **Back Testing of Projections**

Stress Testing

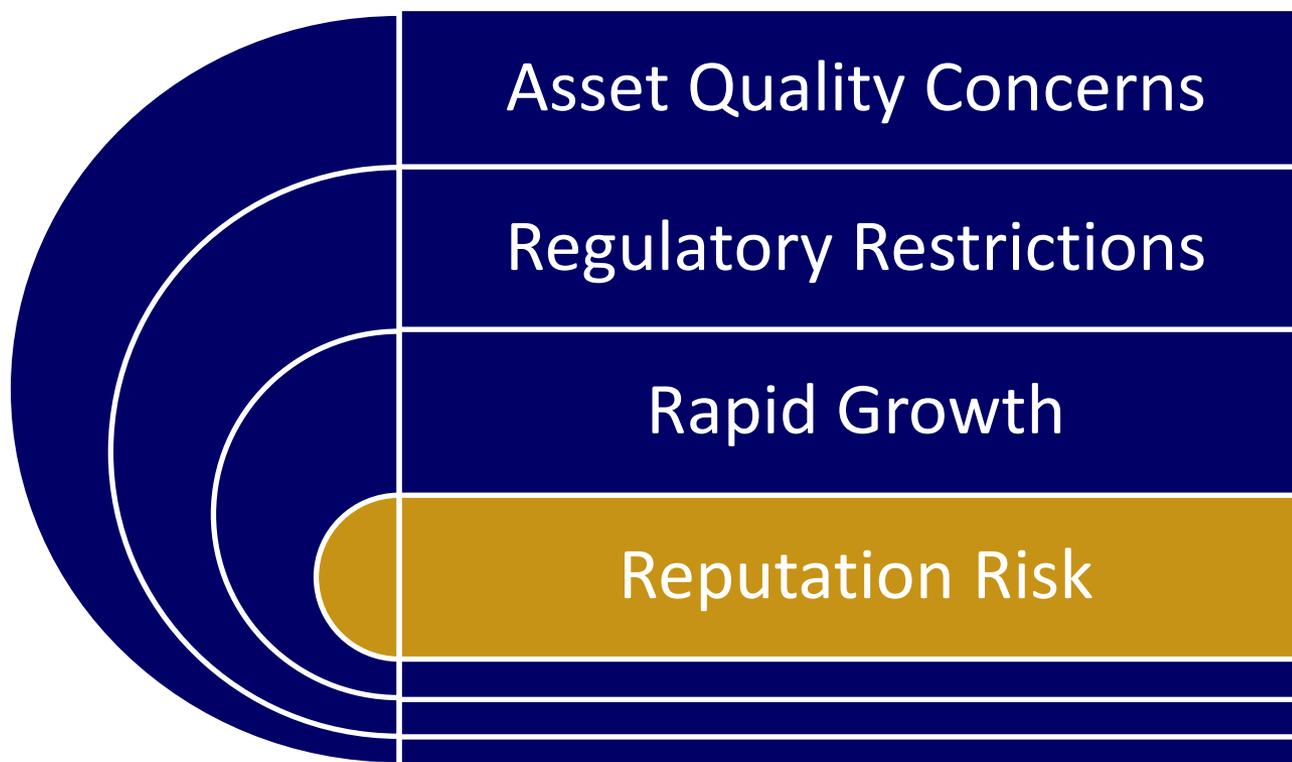


Stress Testing - Expectations

- **Institution-Specific & Market Based**
- **Cash Flow Projections under Adverse Scenarios**
- **Identifies Sources of Liquidity Strain**
- **Sufficient Frequency & Magnitude**
- **Foundation for Contingency Funding Plans**

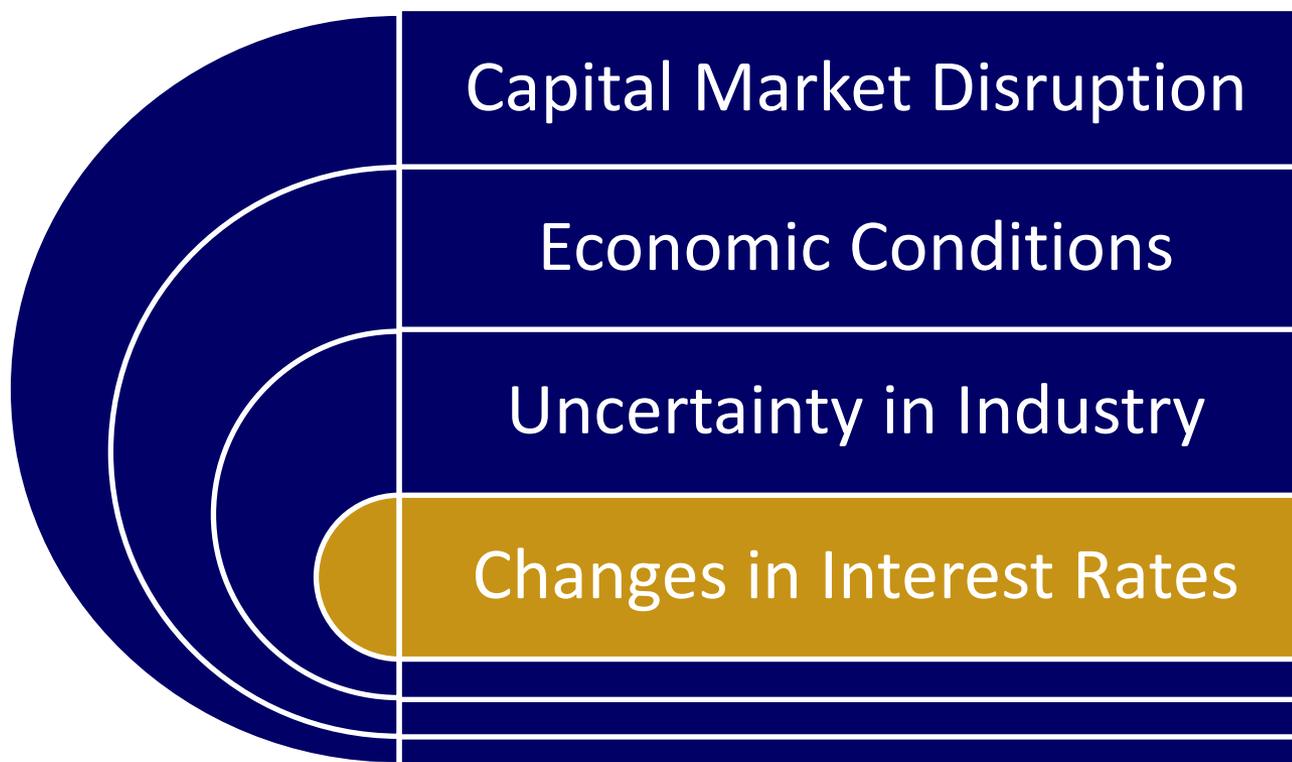
Stress Testing – Adverse Scenarios

Institution Specific Examples



Stress Testing – Adverse Scenarios

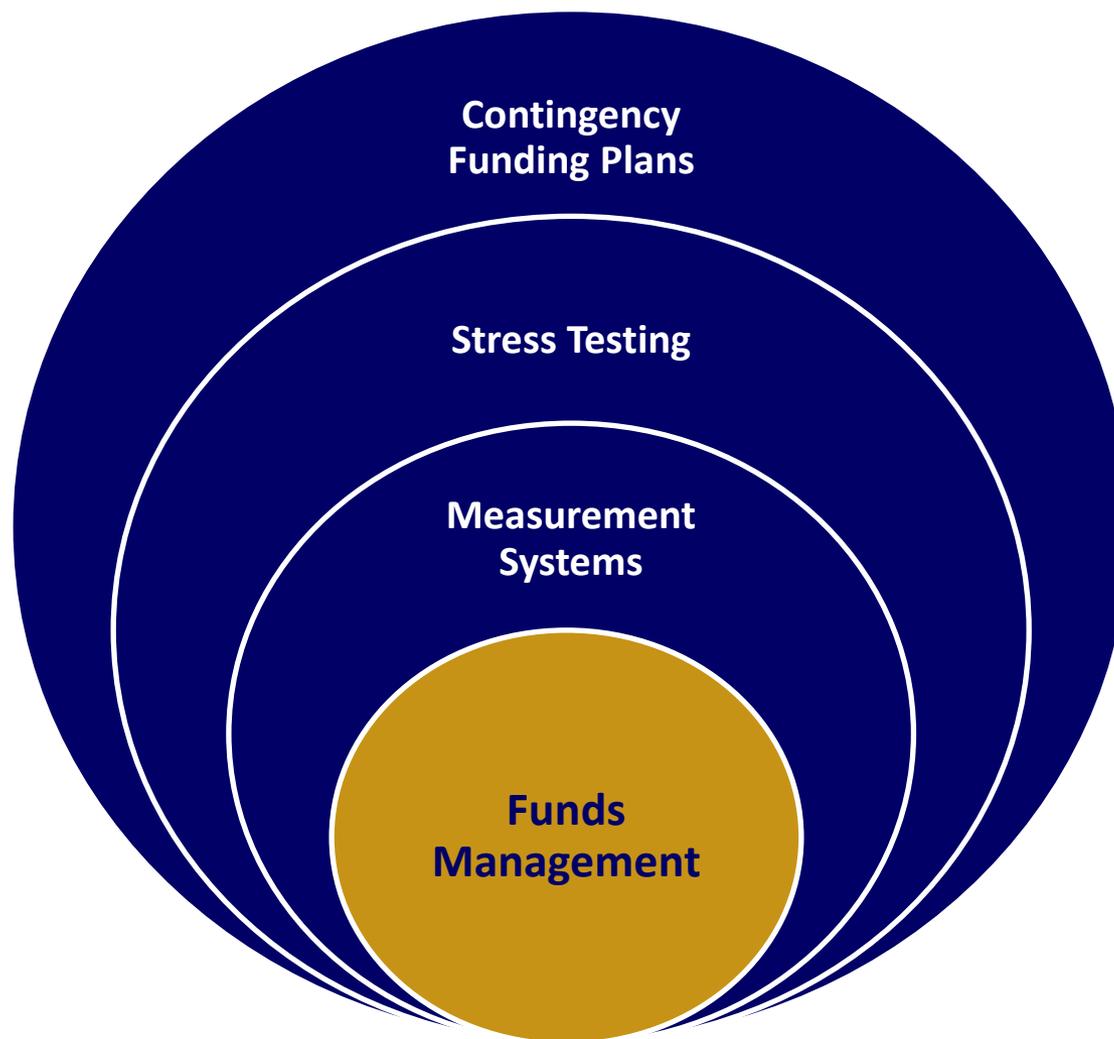
Systemic Examples



Stress Testing – Best Practices

- **Layering in of Mitigating Actions**
- **Reverse Stress Tests**
- **Periodically Model Alternative Stress Tests**

Contingency Funding Plans



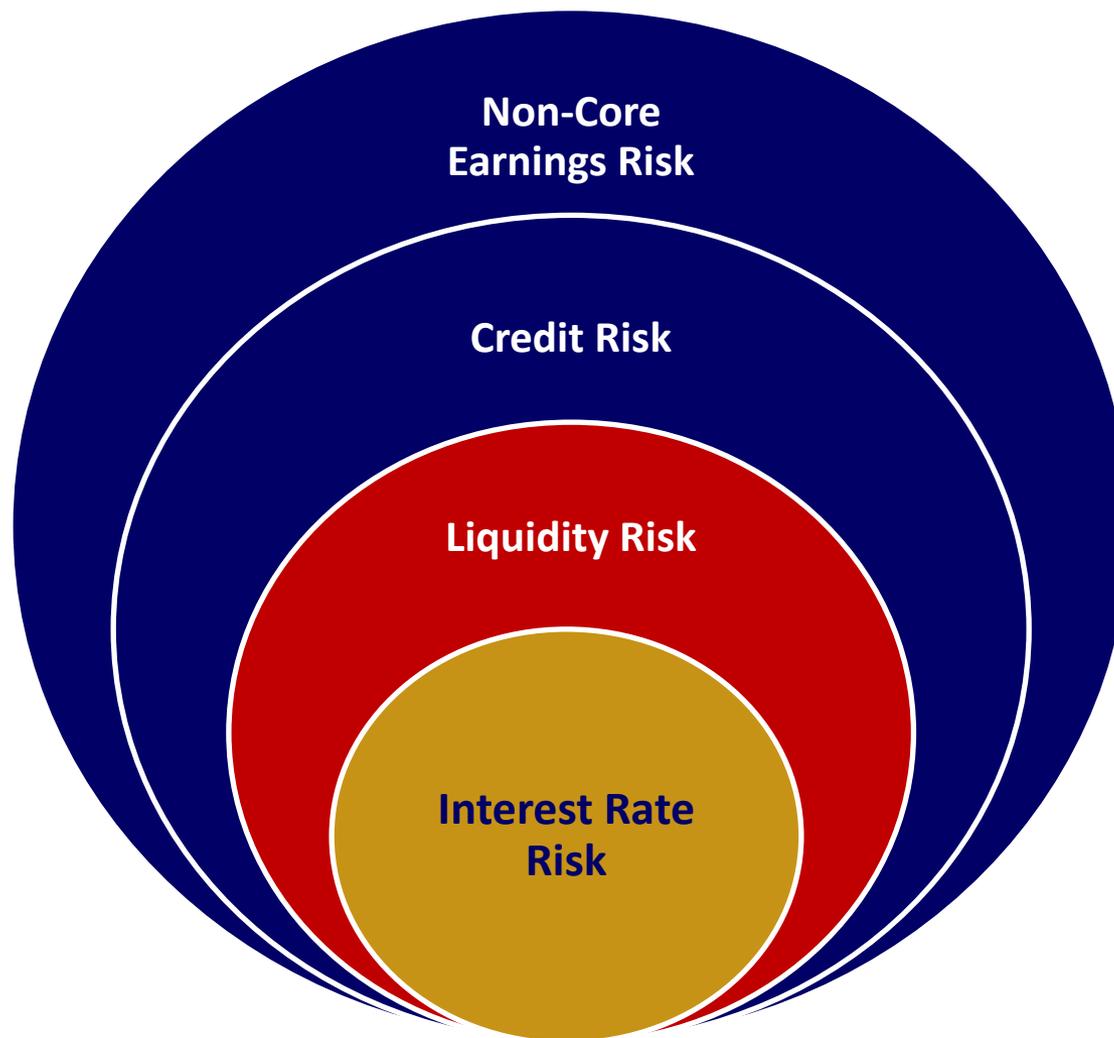
Contingency Funding Plans – Expectations

- **Identify Stress Events**
- **Assess Stress Level and Timing**
- **Assess Funding Sources and Needs**
- **Establish Event Management Process**
- **Develop Action Plans**
- **Establish Monitoring Framework**

Contingency Funding Plans – Best Practices

- **Diversified Funding Sources**
- **Trigger Based Authorities**
- **Conservative Assumptions & Projections**
- **Expect the Unexpected (Testing Action Plans)**

Market Risk – “The Ripple Effect”



Liquidity Effects of Interest Rate Risk

Cash Flows

- Funding Flows & Parked Funds
- Inverse Relationship Between Interest Rates and Mortgage-Related Payments
- Reduced Mortgage Prepayments

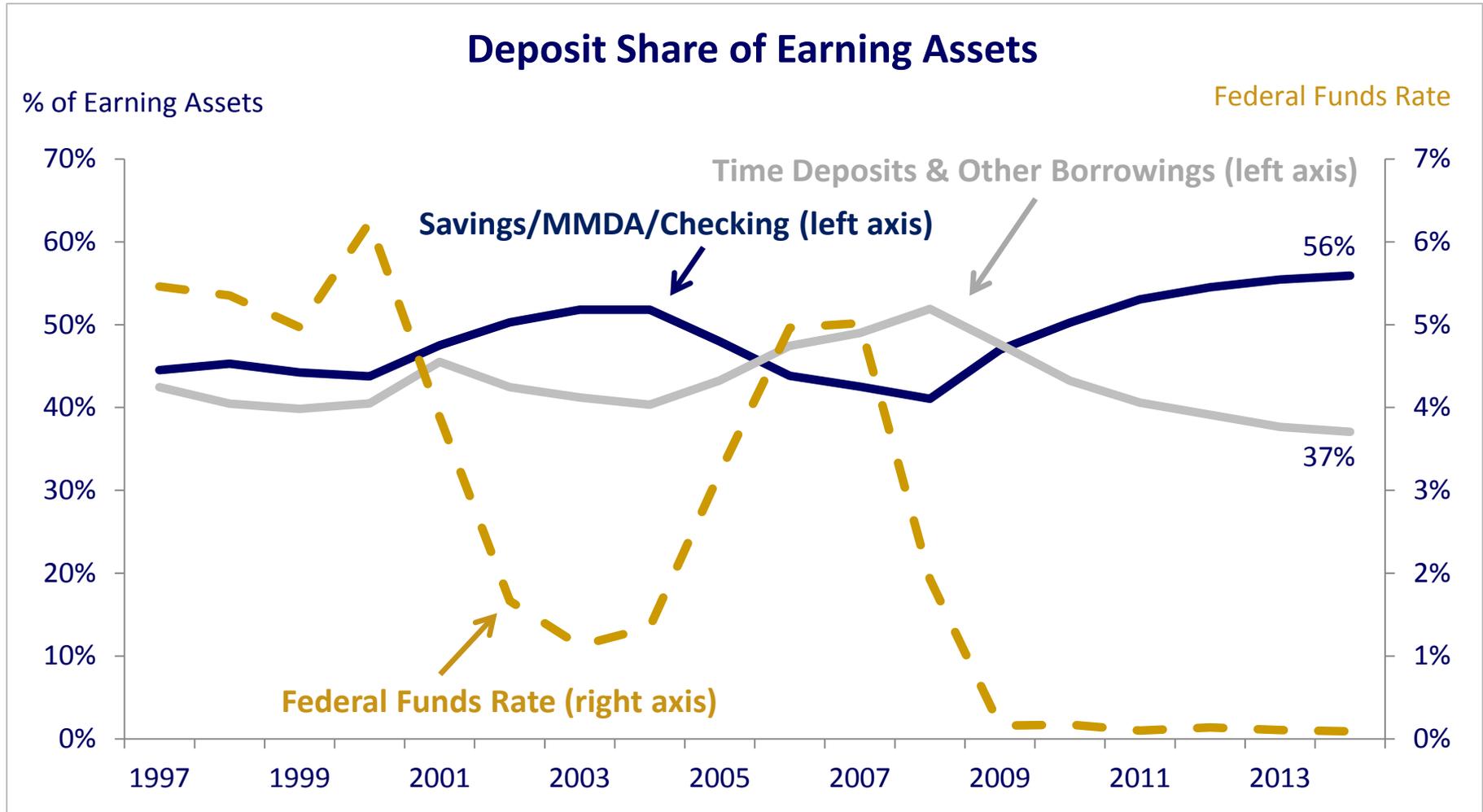
Price Risks

Rate Changes & Mortgage Cash Flows

Rate Changes Can Have Considerable Impact on Prepayment Speeds



Rate Changes & Funding Flows



Source: FDIC Call Reports. Based on median figures of all NY Region banks under \$10B in total assets. Other borrowings includes Fed Funds purchased.

Liquidity Effects of Interest Rate Risk

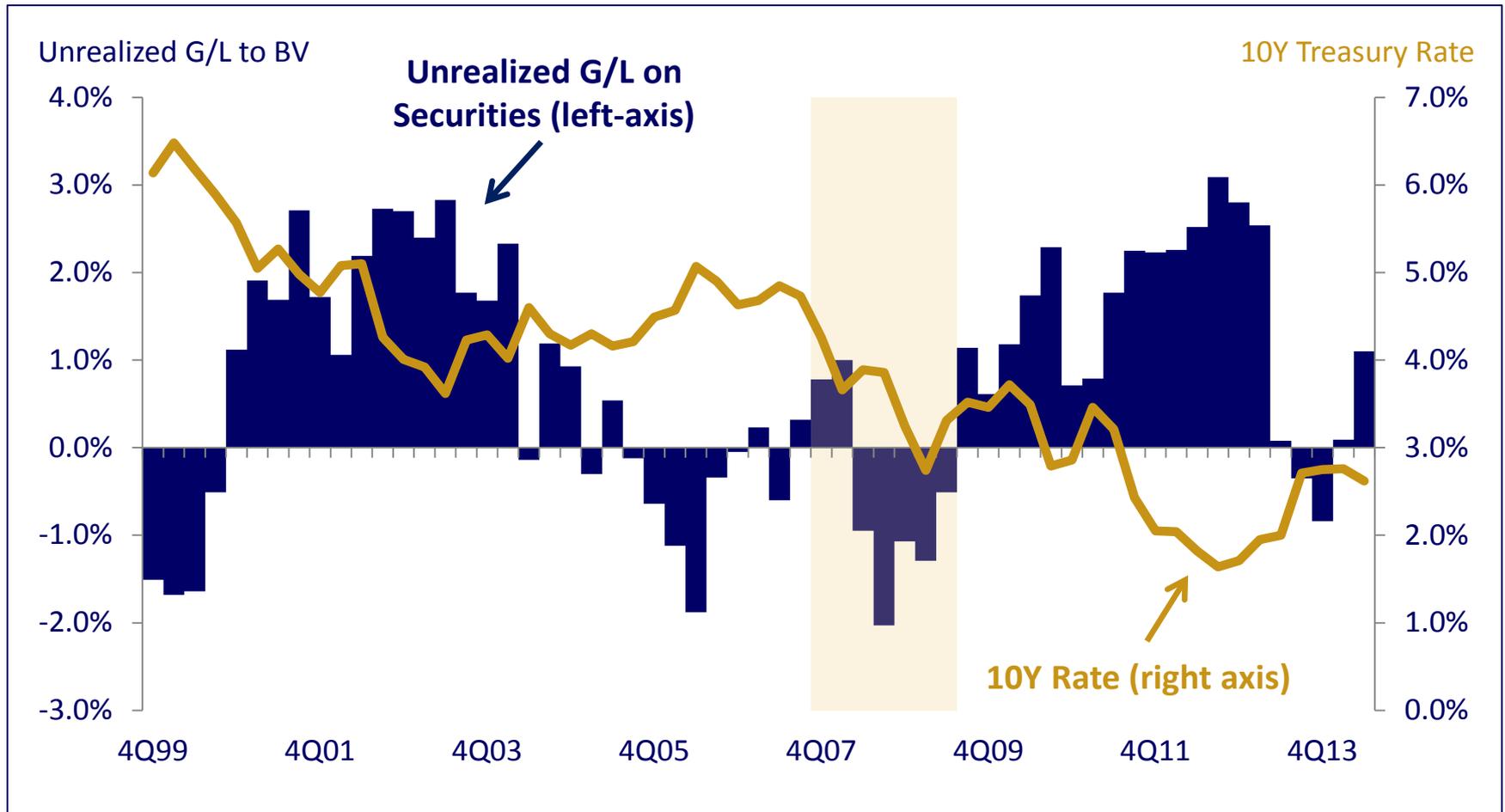
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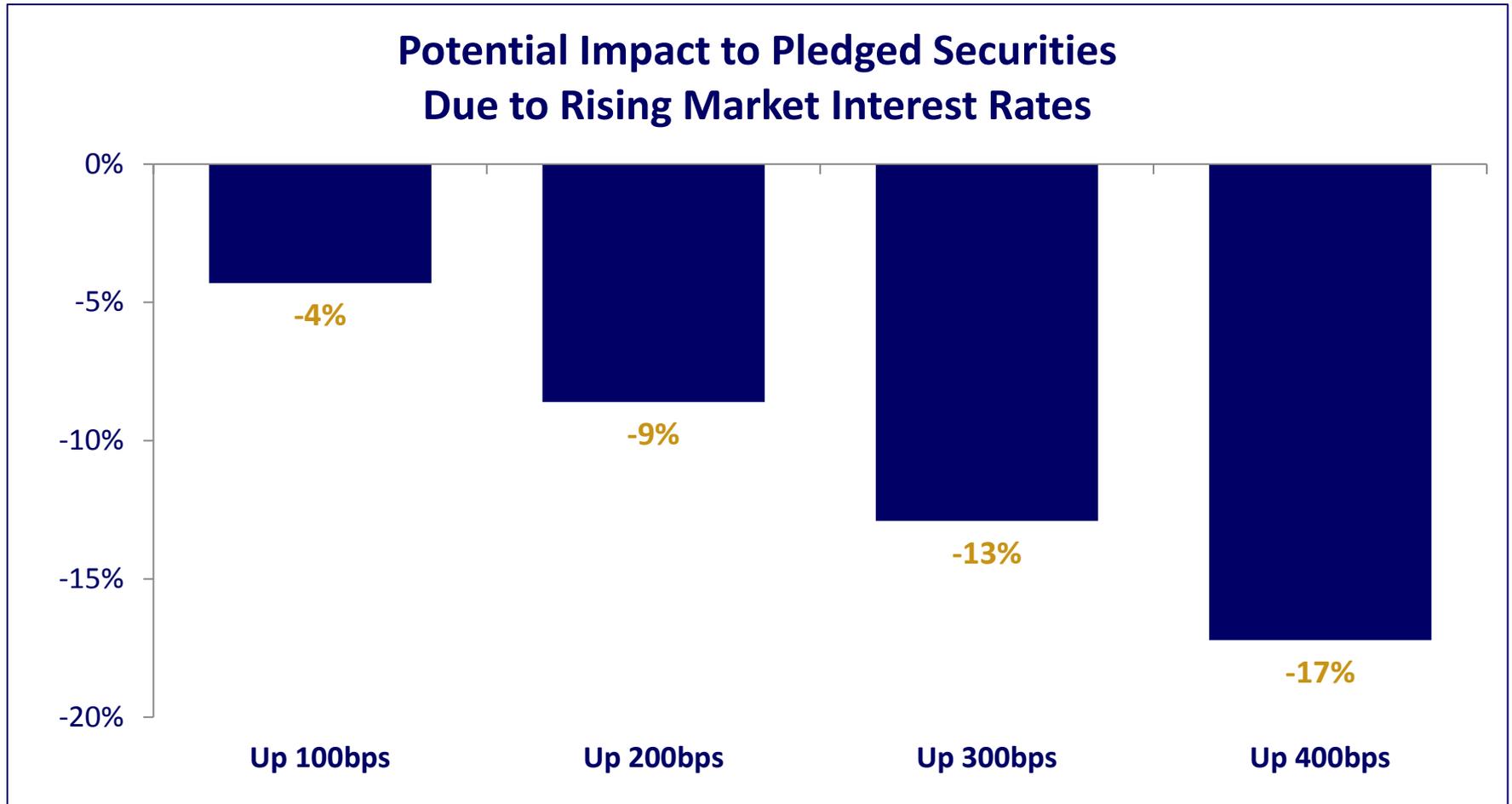
Price Risks

- Inverse Relationship Between Interest Rates and Asset Prices (Valuations)
- Sale-ability Considerations
- Collateral Requirements & Margin Calls

Rate Changes & Price Risks (Valuations)



Rate Changes & Price Risks (Margin Calls?)



Possible Liquidity Risks from Rising Rates



Reduced Mortgage
Prepayments



Reduced Deposit
Levels



Reduced Asset
Valuations



Reduced Borrowing
Capacities

Risk Management Considerations

- **Investment Price Risk Limits**
- **Sources & Uses Calculations**
- **Stress Testing**
- **Contingency Funding Plans**
- **Cushion of Highly Liquid, Unencumbered Assets**

Cushion of Highly Liquid Assets

- **Unencumbered, Readily Saleable**
- **Assess Peak Historic Cash Flow Needs**
- **Add-on for Adverse Liquidity Events**
- **Cushion Should be Established within Policies**

Resources

Outstanding Guidance

- Interagency Policy Statement on Funding & Liquidity Risk Management (FIL-13-10)
- Guidance on Liquidity Risk Management (FIL-84-08)
- Joint Agency Policy Statement on Interest Rate Risk (FIL-52-96)
- Policy Statement on Investment Securities & End-User Derivative Activities
- FDIC Risk Management Manual of Examination Policies

Capital Markets Specialists

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Director's College Program:

Market Risk, "The Ripple Effect"

Director's Resource Center:

www.fdic.gov/resourcecenter

Liquidity Risk & Funds Management

QUESTION & ANSWER OPEN FORUM

Email Questions: NYCalls@fdic.gov

