

# Maryland Financial Bank Advisory Board Meeting

November 4, 2010

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# Agenda

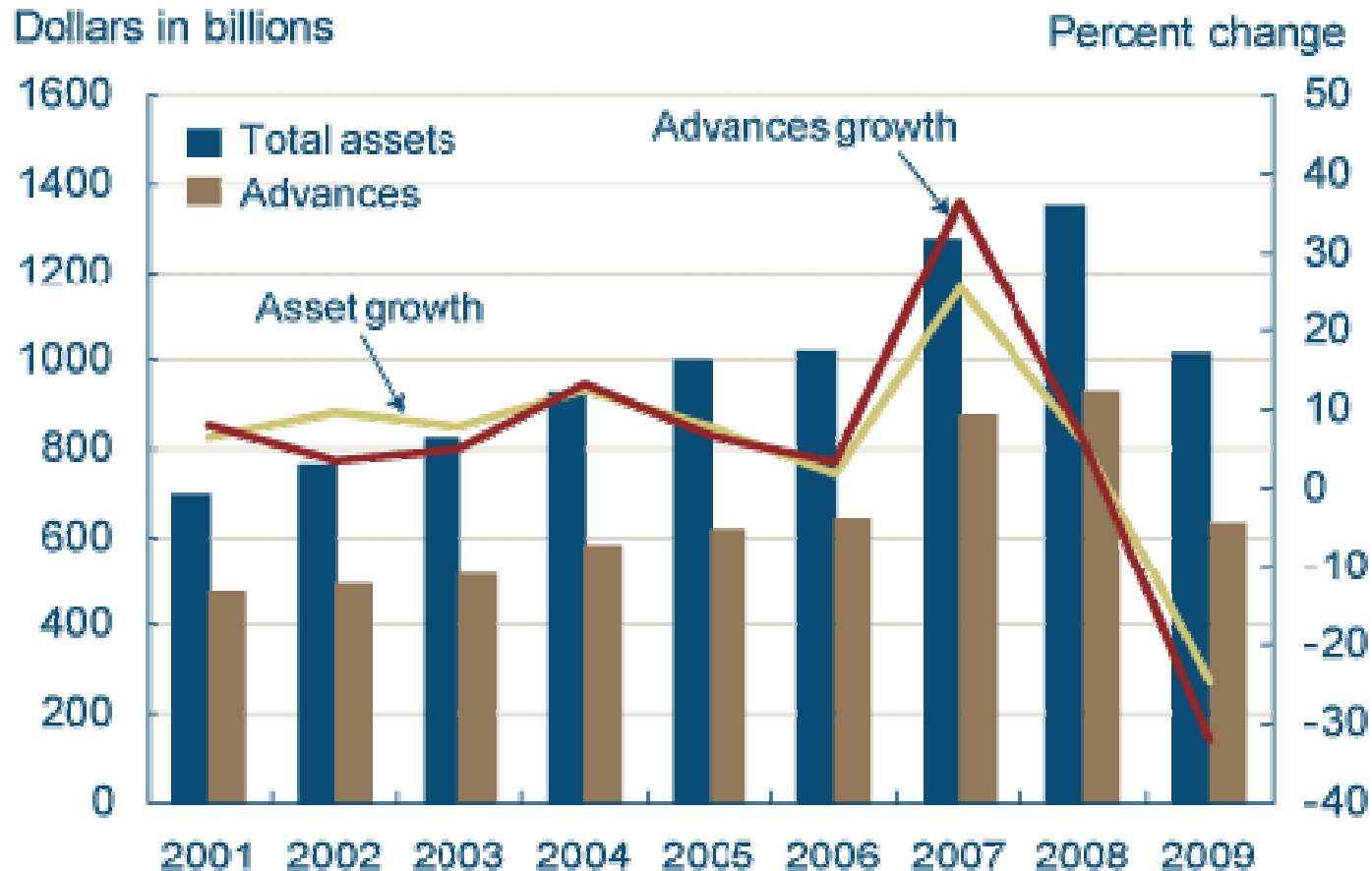


- Update on the FHLBank Atlanta
  - Past
  - Present and Beyond
- Membership Trends – State of Community Banking in the FHLBank Atlanta footprint
- Interest Rate Risk Management
  - Addressing Regulators Concerns
  - Liability Strategies in the Current Environment

# FHLBank System Assets and Advances

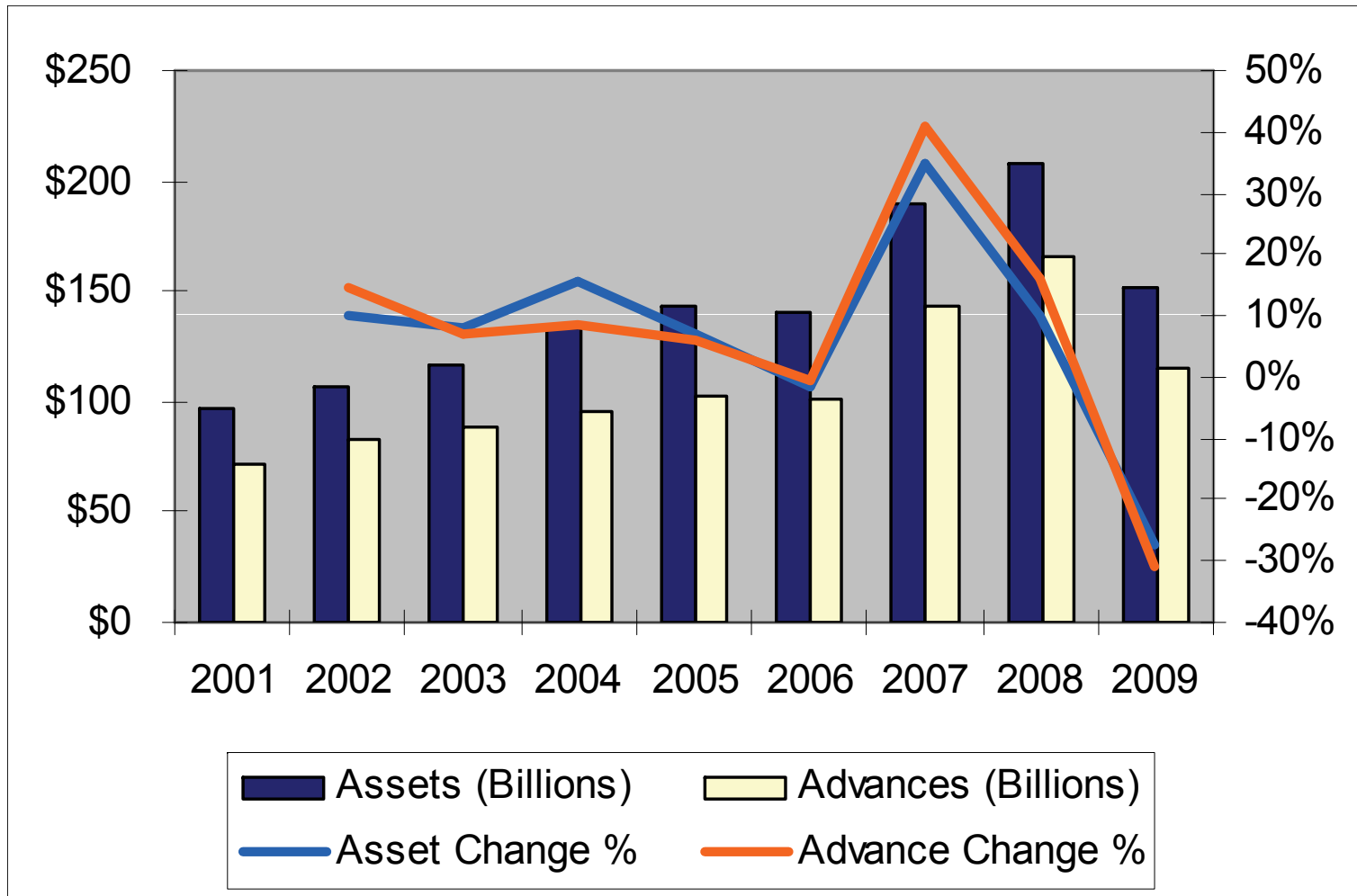


## Federal Home Loan Bank: Assets and Advances



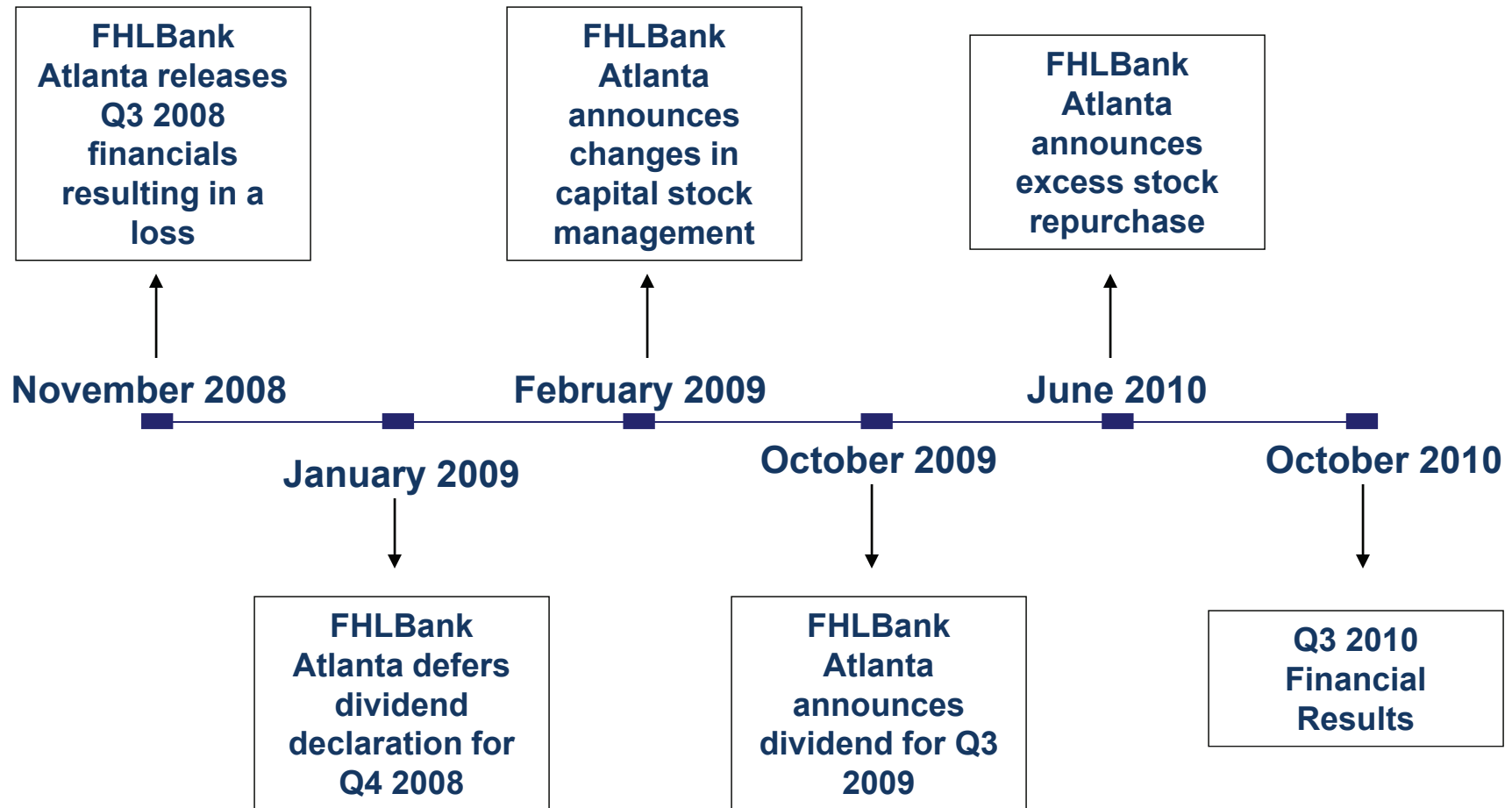
Source: "Federal Home Loan Bank System Annual Reports," 2000-2009.

# FHLBank Atlanta Assets and Advances



Source: "Federal Home Loan Bank System Annual Reports," 2001-2009

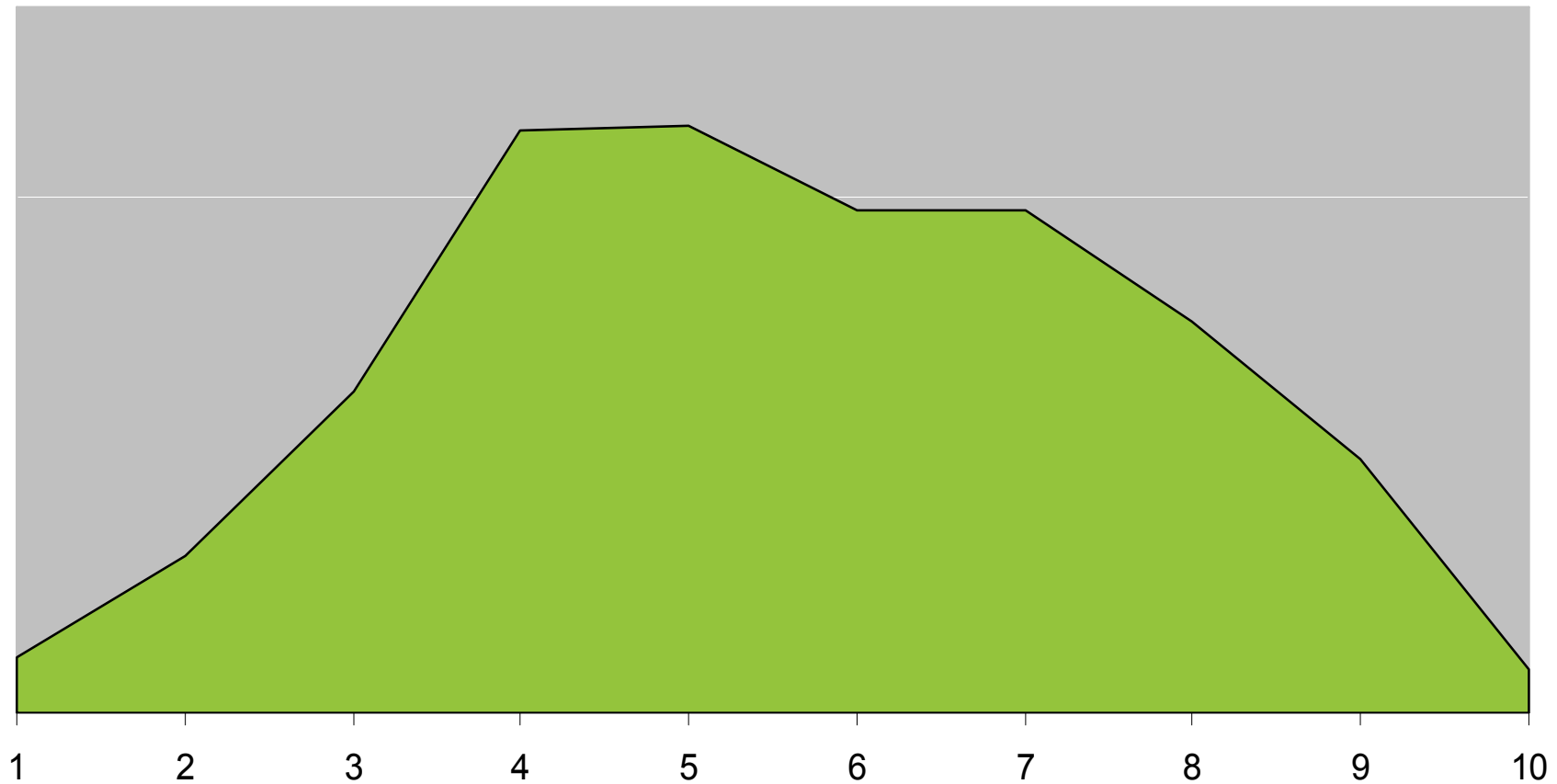
# Timeline of Financial Milestones 2008-2010



## ► Credit Risk Rating Model

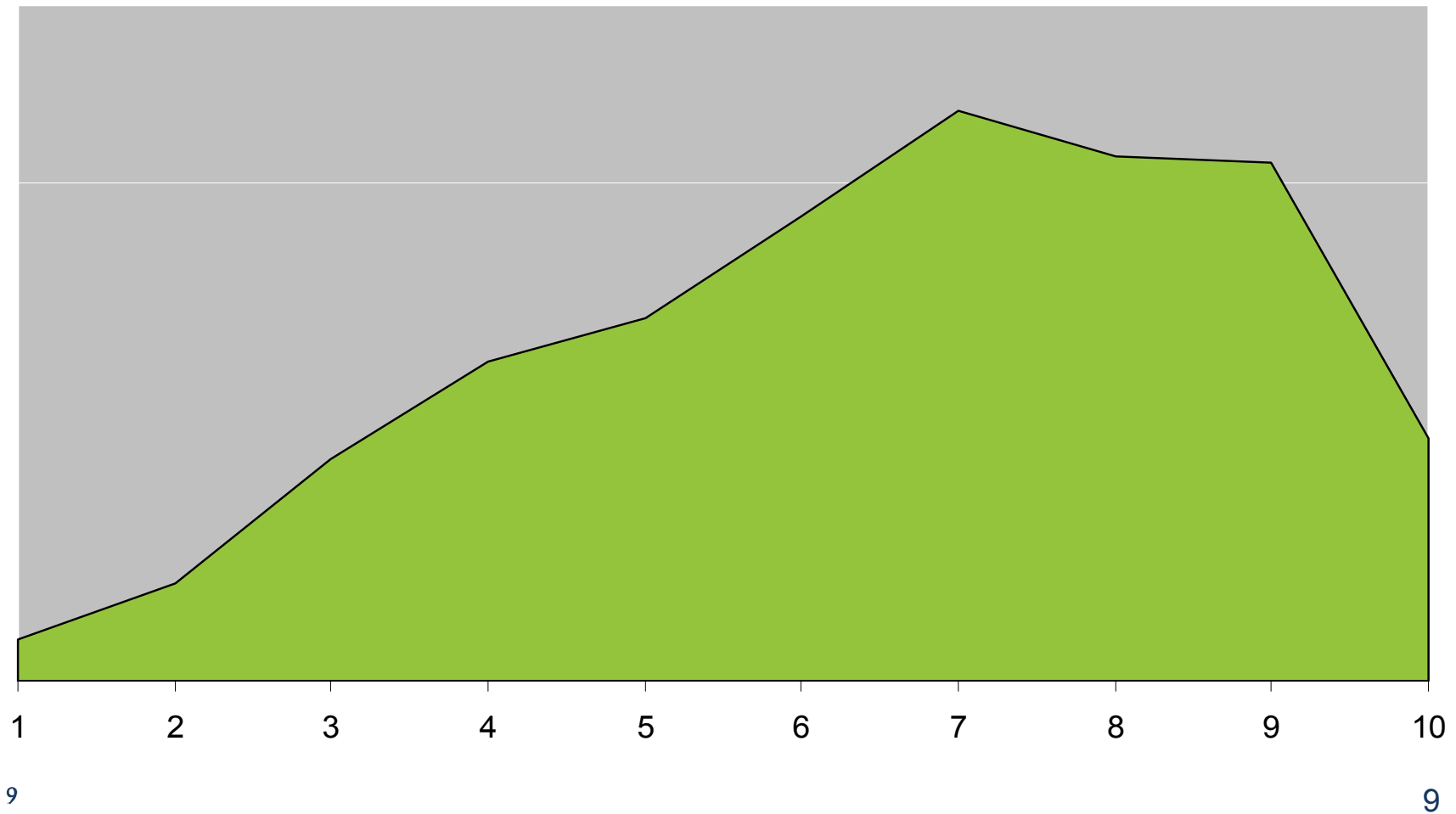
- Model assigns a rating from 1 through 10 (with 1 being the healthiest rating)
  - Based upon increasing probability of default
  - Credit Analysts will review credit ratings each quarter
  - Utilizes 6 key factors
    - Slow Loans: 30+ and non-accruals / total assets
    - Core Capital: core capital / average total assets
    - ROA: 2 quarters net income / total assets
    - Liquidity: government & agencies / total assets
    - Risky Loans: non-residential loans / total assets
    - Asset Concentration: construction, CRE and C&I loans / total assets

## ► 12/31/07 Credit Score Distributions

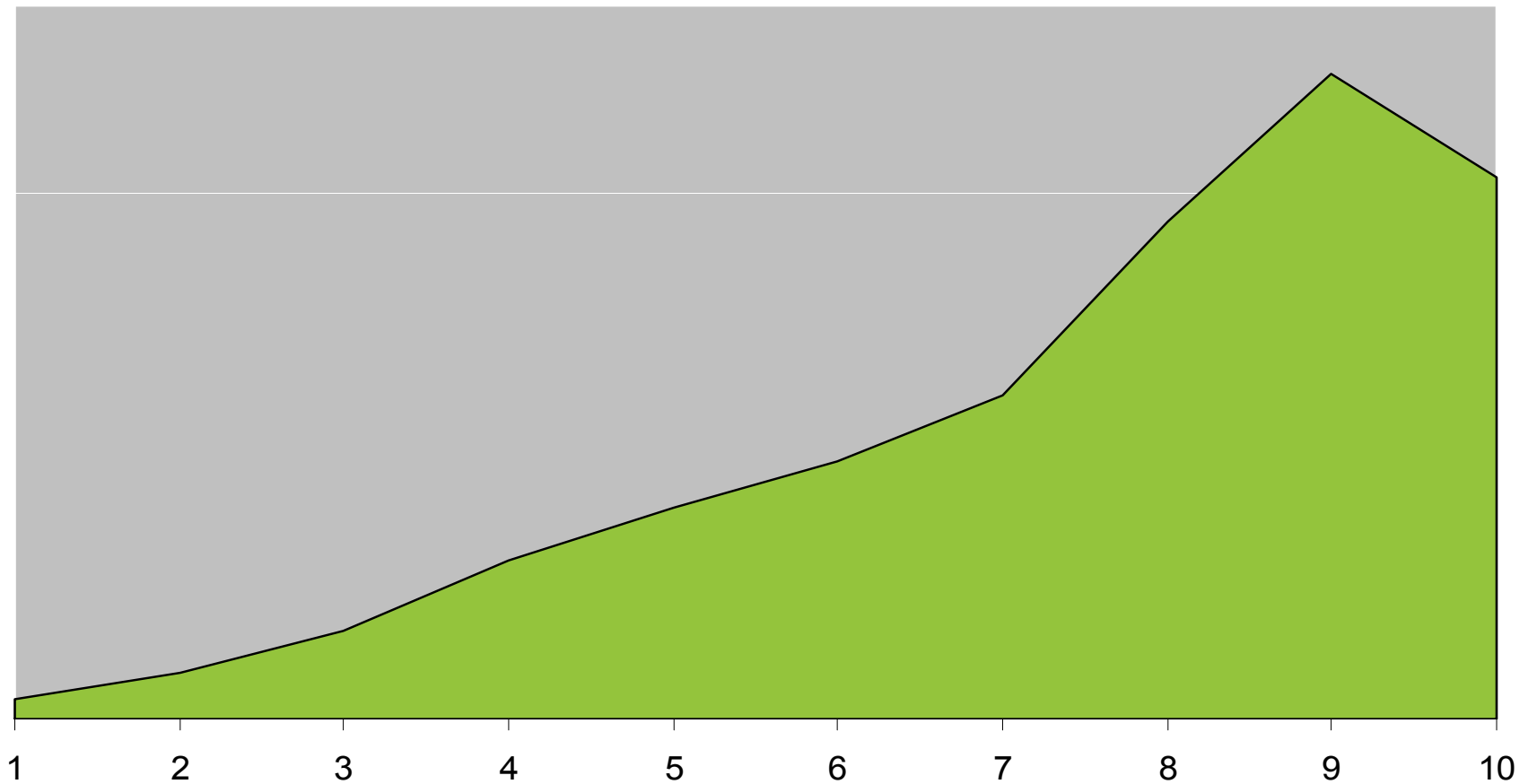




## ► 12/31/08 Credit Score Distributions



## ▶ 12/31/09 Credit Score Distributions



# Strategic Liability Management

# Increased Regulatory Focus

“Failure to maintain an adequate liquidity risk management process will be considered an unsafe and unsound practice.”

## Liquidity Defined:

“A financial institution’s capacity to meet its cash and collateral obligations at reasonable cost.”

## Liquidity Risk:

“Funding mismatches, market constraints on the ability to convert assets into cash or in accessing sources of funds, and contingent liquidity events.”

***Interagency Policy Statement on Funding and Liquidity Risk Management, Federal Reserve Board of Governors, March 2010***

# Managing by Traditional Means

- Purchase liquid securities
- Wholesale Funding Options
  - Brokered
  - FHLB Advances
  - Correspondent lines
  - Repo's
- Core Deposits
  - Mind the franchise
  - Marginal cost considerations

- “In the current environment of historically low short-term interest rates, it is important for institutions to have robust processes for measuring and, where necessary, mitigating their exposure to potential increases in interest rates.”
- “Institutions are expected to have sound risk management practices in place to measure, monitor, and control IRR exposures.”

*Joint Regulatory Advisory on Interest Rate Risk Management, January 6, 2010*

- Assets
- Liabilities
- Derivatives

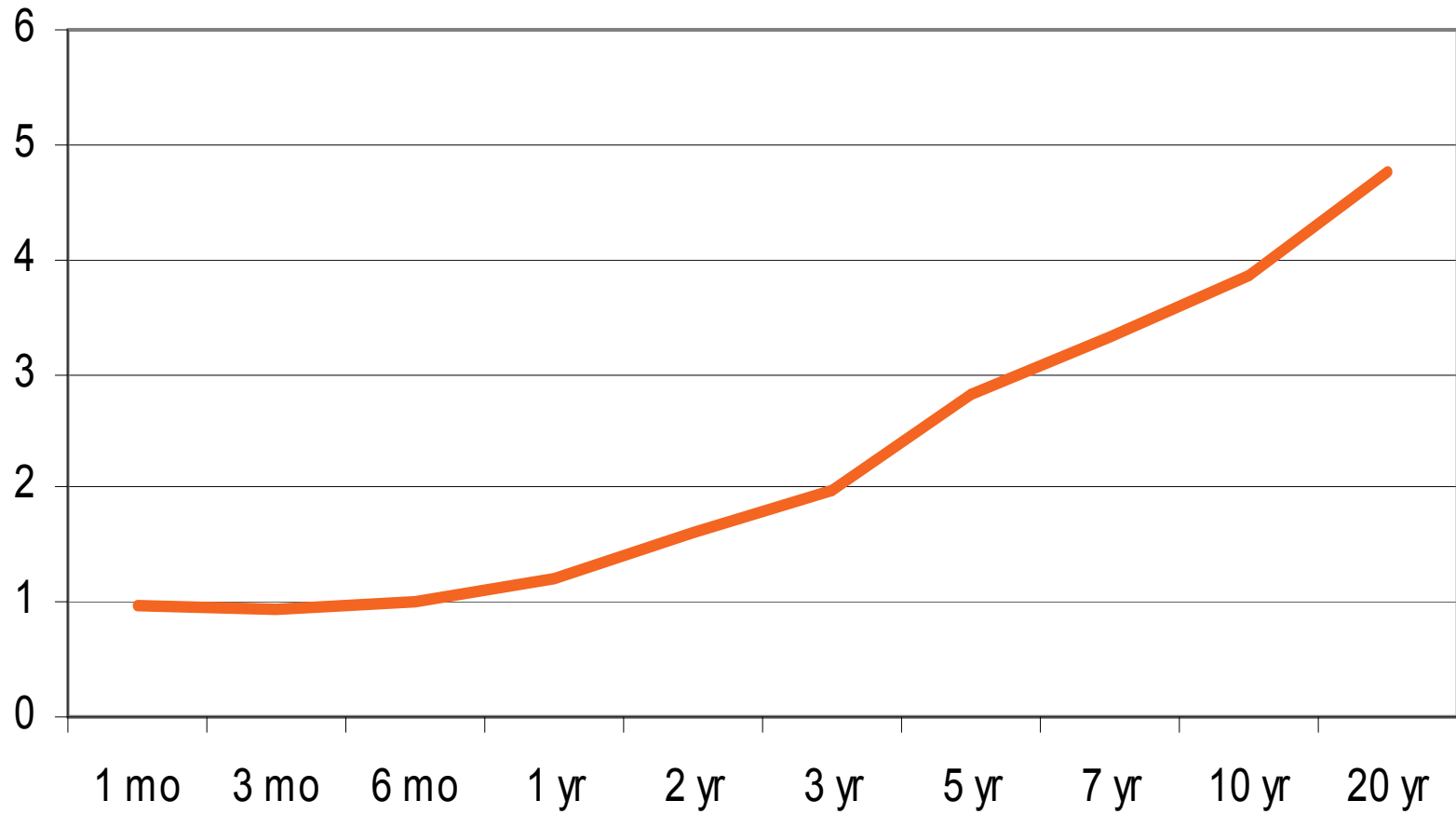
**“In this challenging environment, funding longer-term assets with shorter-term liabilities can generate earnings, but also poses risks to an institution’s capital and earnings.”**

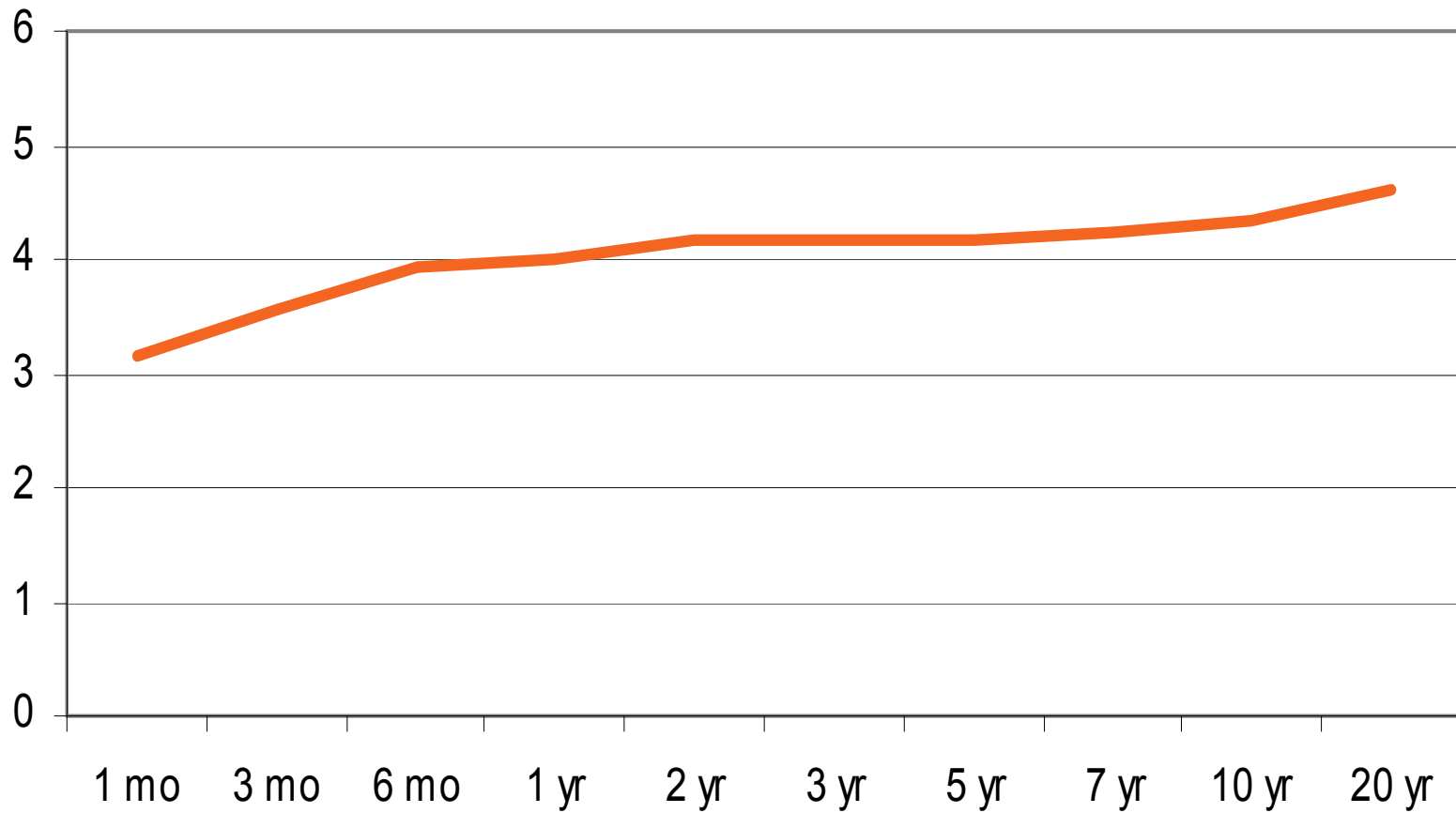
*Joint Regulatory Advisory on Interest Rate Risk Management, January 6, 2010*

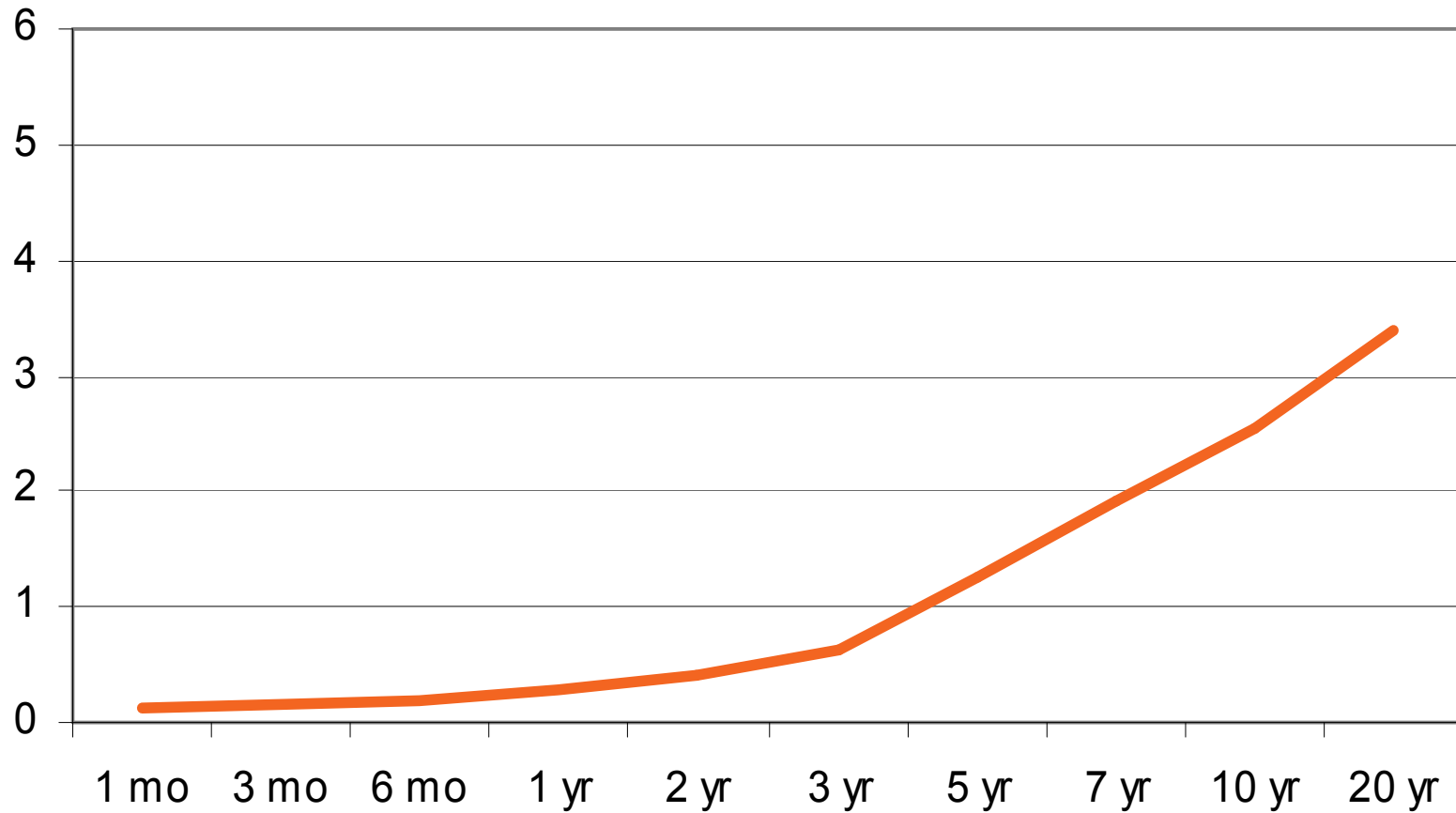
# Heightened Interest Rate Risk

- Shorter duration liabilities
  - Volatile liabilities
- Longer duration assets
  - In-the-money loan floors
- Basis risk
- Current earnings pressure

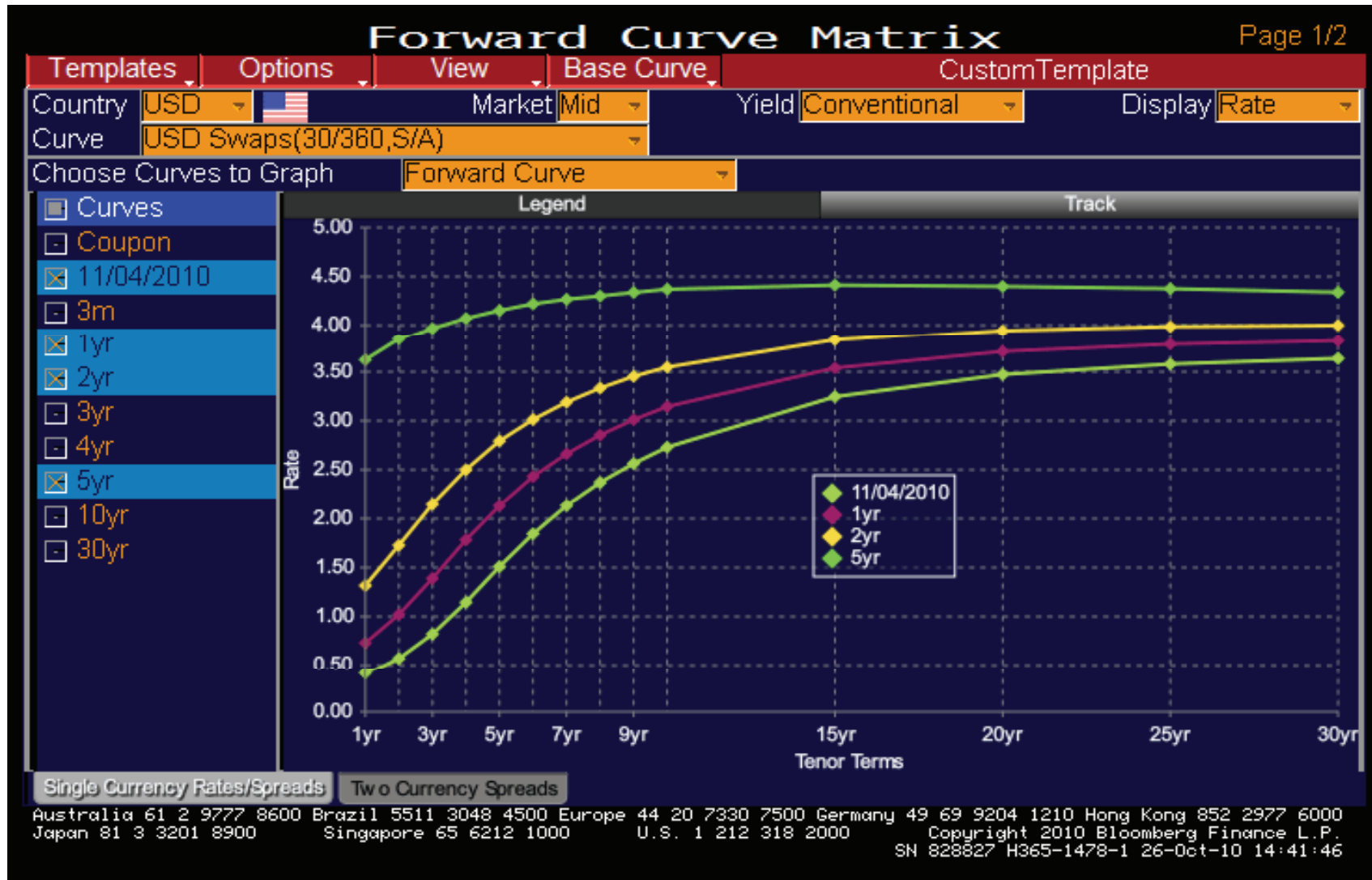








# Market Overview - Forward Curve



- Duration extension
- FRC Hybrid
  - Symmetrical prepay
  - Ladder
- Structure for additional protection
- Pay now or pay later
- Strategic non-core funding
  - Document?

- Term Retail Funding
  - Protect Franchise Value
  - Limited ability to extend
- Brokered Market
  - Increased Flexibility
  - Eliminates “cannibalization risks”
- FRC Hybrid
  - Availability of term
  - Restructure

- Pros
  - Can result in lower interest rate
  - Liability is extended in favorable rate environment
  - Avoids immediate income hit (with applicable accounting treatment)
- Cons
  - “Locks in” the negative NPV

# Restructure Example

- \$10MM, 4.5% rate advance with (\$700M) NPV
- This equals 700 bp
- New 5-year advance
- $700/5 = 140\text{bp/year}$
- Current 5 year rate = 1.57%
- New advance rate = 2.97%



# Enhanced Protection

- ARC with Cap
- FRC Hybrid with Cap
  - Corridor
  - Levered
  - Forward starting

# 3 Month LIBOR Cap Indications



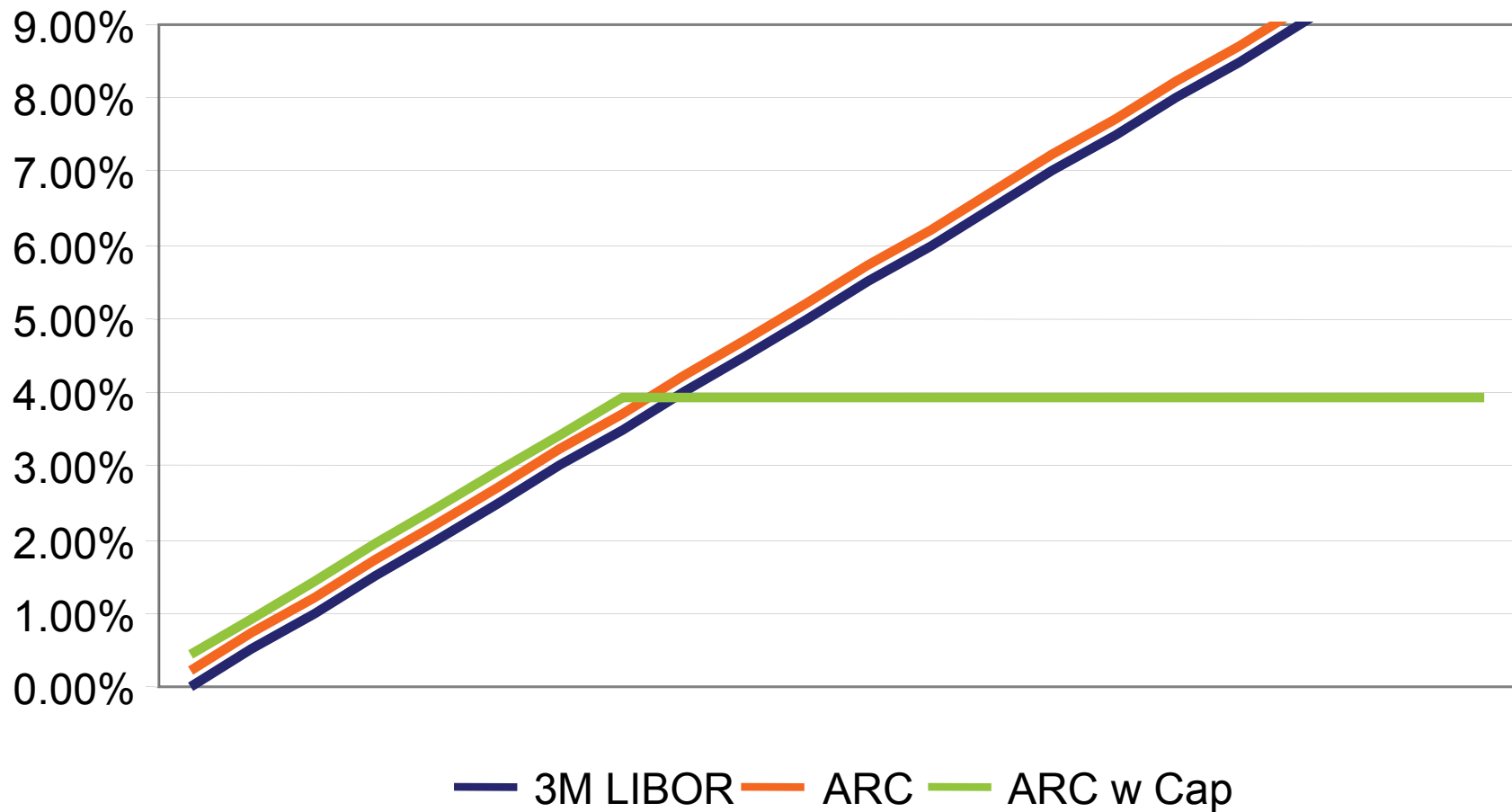
<b>3 Month Libor Caps</b>							
	1 yr	2 yr	3 yr	4 yr	5 yr	7 yr	10 yr
Strike	Running	Running	Running	Running	Running	Running	Running
2.00%	3.0	5.5	13.8	26.0	43.9	84.0	129.0
2.50%	2.9	4.2	10.7	19.9	33.9	67.3	106.9
3.00%	2.8	3.3	8.5	15.7	26.7	53.9	88.0
3.50%	2.6	2.7	7.0	12.7	21.4	43.4	72.3
4.00%	2.5	2.3	5.9	10.6	17.5	35.3	59.5
4.50%	2.4	1.9	5.1	8.9	14.6	29.1	49.4
5.00%	2.2	1.7	4.4	7.7	12.4	24.4	41.4
5.50%	2.1	1.5	3.9	6.7	10.7	20.7	35.3
6.00%	2.0	1.3	3.5	5.9	9.4	18.0	30.5
6.50%	1.9	1.2	3.1	5.3	8.3	15.8	26.7
7.00%	1.7	1.0	2.8	4.8	7.5	14.0	23.7
7.50%	1.6	0.9	2.6	4.3	6.8	12.6	21.4
<b>Advance Rates</b>	<b>0.32</b>	<b>0.53</b>	<b>0.85</b>	<b>1.21</b>	<b>1.57</b>	<b>2.34</b>	<b>3.10</b>

## ARC with Cap

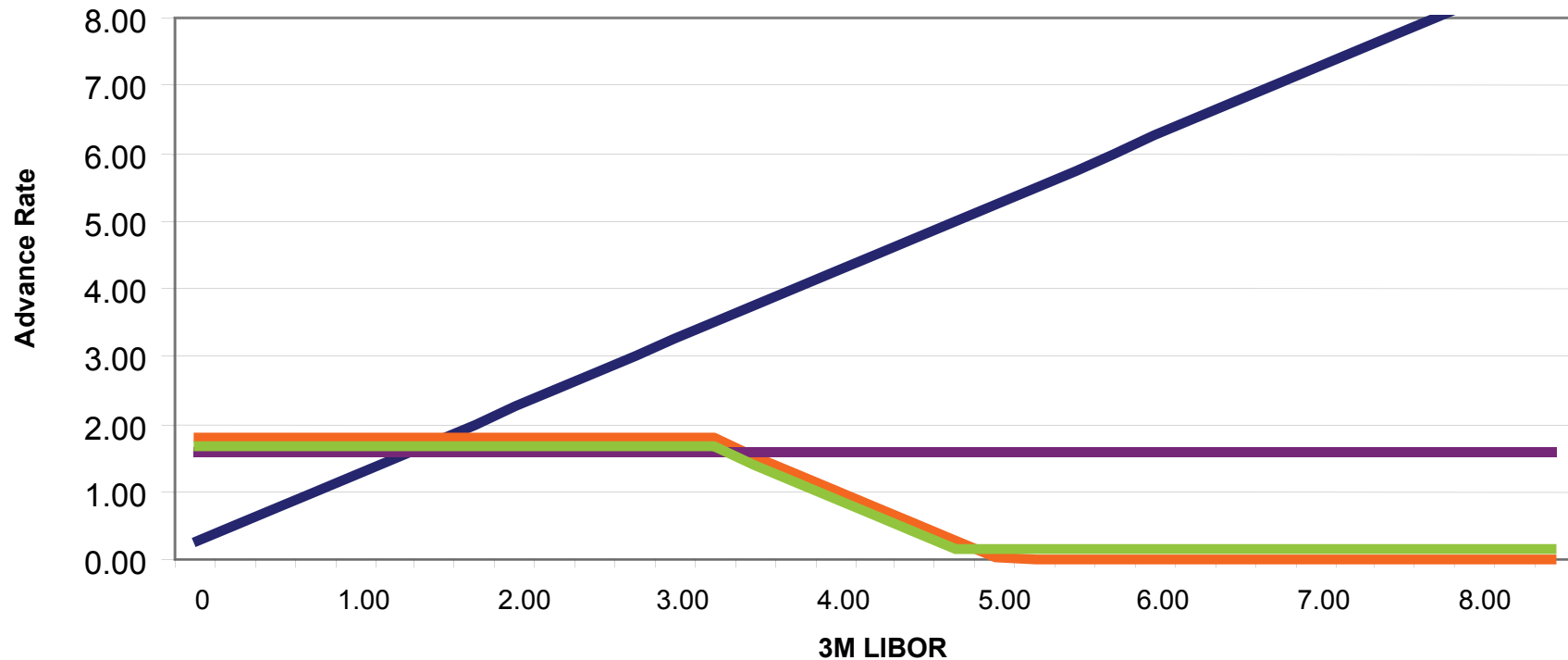
3-month LIBOR	.29%
5yr ARC2 Advance	.22%
Cost of Cap	<u>.21%</u>
Cost of Advance	.72%

Term	5 Years
Strike Index	3-Month LIBOR
Strike Rate	3.50%
Annual Cost	21 bps

## ARC with Cap



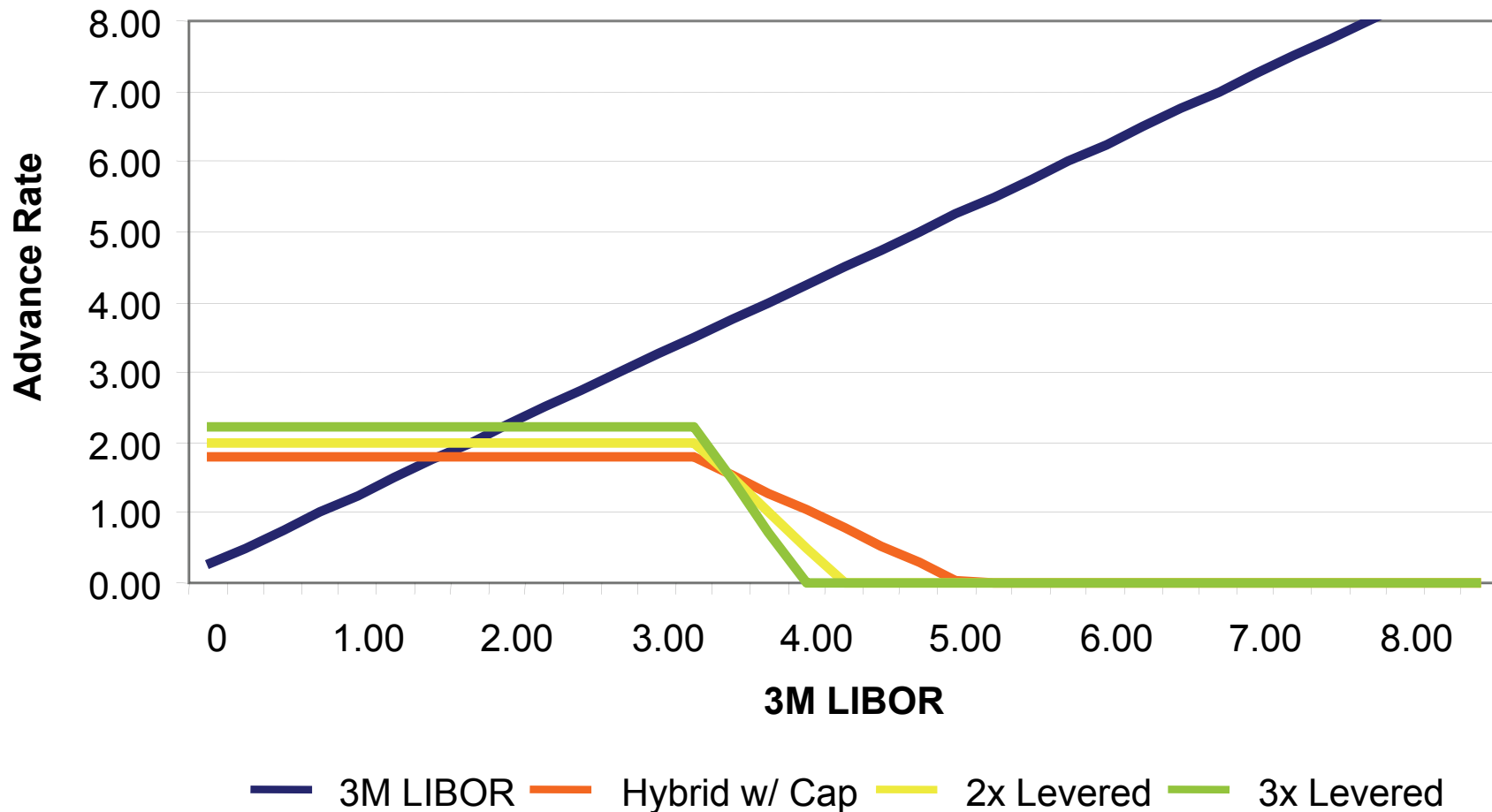
## FRC Hybrid with Cap



— 3M LIBOR  
 — Hybrid w/ Cap  
 — FRC Hybrid  
 — Cap Corridor

5 year Hybrid	1.57%
3.50% Cap	<u>.21%</u>
Advance Cost	1.78%
(Less 5% Cap)	<u>-.12%</u>
Corridor Cost	1.66%

## FRC Hybrid with Levered Caps





# Questions?

Sales and Trading