Introduction to ALM

Lisa Boylen
VP, ALM Services
First Carolina Corporate Credit Union
Introduction

• **Lisa Boylen**
  - First Carolina Corporate Credit Union
    VP, ALM Services - 6 years
  - Community Banking accounting/finance/ALM – 20 years
  - North Carolina Licensed CPA
Outline

• Orientation to Financial Performance
• Role of Asset Liability Management
Business Perspective

• Buy and sell money – financial intermediary

• Objectives
  • Serve Members
  • Grow membership base – loans and shares
  • Generate a profit to preserve capital

• Manage risks
  • Credit Risk
  • Interest Rate Risk
  • Liquidity Risk
Financial Statements

• **Balance Sheet**
  - Statement of Assets Owned, Liabilities Owed and Capital as of a point in time

• **Income Statement**
  - Statement of Earnings over a period of time

• **Ratios**
  - Relationship between income statement and balance sheet.
  - Good measure of financial performance and allows comparisons with other credit unions regardless of size.
# Financial Statements Samples

<table>
<thead>
<tr>
<th>Balance Sheet</th>
<th>Avg Balance</th>
<th>Yield</th>
<th>YTD Inc/Expense</th>
<th>Income Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash &amp; Equivalents</td>
<td>27,510,392</td>
<td></td>
<td></td>
<td>Investment Income</td>
</tr>
<tr>
<td>TOTAL INVESTMENTS</td>
<td>20,510,505</td>
<td>1.32%</td>
<td>270,544</td>
<td>Loan Income</td>
</tr>
<tr>
<td>TOTAL LOANS</td>
<td>88,050,561</td>
<td>8.49%</td>
<td>7,473,964</td>
<td>Interest Income</td>
</tr>
<tr>
<td>Total Earning Assets</td>
<td>108,561,066</td>
<td>7.13%</td>
<td>7,744,508</td>
<td></td>
</tr>
<tr>
<td>(Allowance for Loan &amp; Lease Losses)</td>
<td>-573,714</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>All Other Assets</td>
<td>6,991,899</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTAL ASSETS</td>
<td>142,489,643</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| LIABILITIES & CAPITAL:     |              |          |                 |                        |
| TOTAL SHARES & DEPOSITS    | 122,799,549  | 1.70%    | 2,093,532       | Interest Expense       |
| TOTAL LIABILITIES          | 48,495       |          |                 |                        |
| TOTAL EQUITY               | 19,641,299   |          |                 |                        |
| TOTAL LIABILITIES, SHARES, & EQUITY | 142,489,343 | | | |

<table>
<thead>
<tr>
<th></th>
<th>5.43%</th>
<th>5,650,976</th>
<th>Net Interest Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.47%</td>
<td>674,360</td>
<td></td>
<td>Provision for Loan Loss</td>
</tr>
<tr>
<td>1.22%</td>
<td>1,732,604</td>
<td></td>
<td>Non-interest Income/Avg Assets</td>
</tr>
<tr>
<td>3.46%</td>
<td>4,928,832</td>
<td></td>
<td>Non-Interest Expense/Avg Assets</td>
</tr>
<tr>
<td>-0.08%</td>
<td>(118,450)</td>
<td></td>
<td>Non-Operating Inc/(Exp)</td>
</tr>
<tr>
<td>1.17%</td>
<td>1,661,938</td>
<td></td>
<td>Net Income (Loss)/ROA</td>
</tr>
</tbody>
</table>

*First Carolina Corporate Credit Union*

Primary Drivers of Financial Performance

- Net Interest Income
  - Mix of Assets and Liabilities
  - Pricing of Assets and Liabilities
  - Volume of Assets and Liabilities
  - Interest Rate Risk
- Provision for loan loss
- Sources of non-interest income
- Operating Expense efficiency
- Non-operating income/expense
Role of Asset Liability Management
What is It?

An ongoing process of managing assets and liabilities to meet financial objectives, while balancing risk with reward.
Asset Liability Management

• **Ongoing Process**
  - More than a one-time compliance event to meet regulatory expectations

• **Managing**
  - Evaluation and taking action
  - Selecting and pricing assets and liabilities
  - Determining asset/liability composition

• **Financial Objectives**
  - Integrated with the credit union’s goals and objectives

• **Balancing Risk with Reward**
  - Not designed to eliminate risk
  - Choosing the risk/return trade off that is optimal for the credit union
Goal of ALM

① Maximize Earnings
② Protect Capital
③ Maintain stability of earnings and capital
④ Ensure adequate liquidity to meet member withdrawals, funds loans and meet operating expenses.
⑤ Balance Risk and Reward
ALM Decisions and Constraints

**Assets**
- Loans
- Investments
  - What Price?
  - What Term?
  - How Much?

**Liabilities/Capital**
- Share Accounts
- Certificates
- Borrowings
  - What Price?
  - What Term?
  - How Much?

**Competition**

**Economy**

**Regulatory Environment**
ALM Process

• Develop policy and establish risk tolerance guidelines
• Measure the risk and rewards of the credit union’s balance sheet
• Monitor how it changes
• Adjust balances and pricing to improve its risk/return tradeoff

IT IS AN ONGOING PROCESS
Keys to a Successful ALM Process

• Active Board & Senior Management Oversight
  - Understand the amount and type of risk

• Adequate Policies & Limits
  - Guidelines to Control Risk-taking

• Risk Monitoring Systems
  - Identify and measure risk

• Adequate Internal Controls
Board of Directors’ Responsibilities

• Oversight of the ALM process
• Approve ALM policy
• Understand Amounts and Types of Risk
• Set risk tolerances to maintain earnings and protect capital as interest rates change
• Assign responsibilities
• Monitor risk through management reporting
ALCO Responsibilities

• Develop and implement policies
• Determine and recommend strategic balance sheet plan
• Develop risk monitoring systems to identify and measure risk
• Monitor risk and plan process
• Develop specific actions to implement balance sheet plan and control risk
• Communicate with Board
Review Questions

ALM is a one-time compliance event to meet regulatory expectations.

- True
- False
The goal of ALM is to?

- Balance Risk & Reward
- Protect Capital
- Maximize Earnings
- Ensure Adequate Liquidity
- All of the Above
Review Questions

Your responsibility as a Board Member is to?

- Oversee the ALM process
- Approve ALM policy
- Establish Risk Limits
- Monitor Risk Position
- All of the Above
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