TAKING AIM AT THE FUNDAMENTALS OF LIQUIDITY

by Steve Brown

There is more to goal setting than just setting a random target. Consider research from Harvard that finds people who set too many goals tend to focus on hitting the ones that deliver the greatest quantity vs. the greatest quality. The key to successfully setting goals is to keep them realistic and attainable, but also specific enough so you can measure success as you move forward. It also takes time for new things to become a routine, so be sure to give yourself enough to establish a solid one. Writing down 3-5 goals you want to achieve and attaching a timeline to each one will help you stay focused and improve your odds of achieving them. Be sure to set and stick to deadlines to make sure you reach your goals, but allow yourself just enough flexibility to adjust to a changing schedule. Stay focused, keep your list of goals front and center, pick just a few and you are onto something powerful. When it comes to setting goals, one area banks might want to review is liquidity. Yes, we know there is plenty of liquidity in the system right now and plenty of other things to do. However, that also means you have lots of time to get a handle on your liquidity situation before the massive pool eventually begins to dry up. One place to start is by leveraging work already done by Basel. You don't even have to know or care who Basel is or what it stands for, but know it is the source for all global banking regulations worldwide, so it can be leveraged. Setting targets when it comes to liquidity begins at the purest level. Begin by identifying all bank assets that can be converted into cash at any time (particularly during periods of significant market stress). This is the most liquid pool in your overall plan, so it is important to get it right. Be completely honest when your management team does this, as your goal is to fully understand how much immediate liquidity you have. Don't overestimate what you can convert to cash - make absolutely sure before including it in the number. Now that we have identified this first pool of immediate liquidity, we move to the next. Here, Basel indicates banks should identify "high quality liquid assets." These are defined as assets that are traded in large, deep and active markets; have a proven record as a reliable source of liquidity (even during stressed market conditions); and are eligible to be borrowed against at the Fed (or other central banks worldwide). Additionally, they are not assets issued by or are an obligation of a financial institution or any of its affiliated entities. Now that you have identified all of your high quality liquid assets and have challenged each one before you put it into the bucket, you have a solid percentage of the assets you can turn into cash and that are highly liquid. Once you have that, you can begin to track things over time and determine whether you have enough liquidity or need to begin increasing it. Now it is time to track and report. Here, you want to add a section to your board package that tracks and reports monthly on your funding concentrations. Use the 80/20 rule and list the Top 10 accounts and how much funding they provide as a percent of total assets. This will highlight how much the bank relies on a discrete group of funding sources and what you would have to do on the asset side (shrink or sell), if it walked out the door tomorrow. Once you know that, you can work up a contingency plan, extend the maturity of this funding to protect against short term swings and make sure you have room in your asset structure to handle liquidity issues that may surface. Assets should be liquid and be easily borrowed against or sold in an emergency situation. We will cover this topic again in the future, but hopefully these few steps set a target to aim for as you begin the process.

BANK NEWS

Restructuring

SunTrust reported it did some major adjusting to its balance sheet, as it moved to address issues that had been dogging the bank for years. SunTrust sold the rest of its holdings in Coca-Cola for a $1.9B pre-tax gain, took a $375MM provision for mortgage repurchase losses, wrote off $3B in bad loans, and sold $200mm in affordable housing investments. All told, the bank expects to see a net gain of $750mm.

Fed Connection

The Fed has launched "Community Banking Connections," a publication and online resource for community banks designed to clarify supervisory guidance; highlight new regulations; provide perspectives from bank examiners / Fed staff; and address community bank concerns.

Gift Cards

Safeway plans to take its popular gift card business Blackhawk Network Holdings Inc., public sometime in 2013. Safeway has the 3rd largest third party distribution company in the country, selling gift, phone, and retail cards.

Mooning Risk

A judge has ruled a Bank of America executive fired in 2005 (after getting angry with his bosses, he pulled down his pants and mooned them) was "insubordinate, disruptive, unruly and abusive." As such, the judge said he was not entitled to a multi-million dollar contingent bonus package that would have vested if he had remained at the company a few more months. The moral: keep your pants on no matter how angry you get.