Liquidity And Capital Management During COVID-19

liquidity pandemic capital management

Summary: During this pandemic crisis, financial institutions should evaluate liquidity and capital management models and policies. Also, make sure to stress your liquidity projections to evaluate adverse and severe scenarios.

During this pandemic crisis, it is imperative that bankers remain cognizant of all changes in directives and rules affecting our industry to properly manage liquidity and capital. These rules and statements are coming fast and furious almost every day, so keeping up is very difficult right now. We are providing the information as it comes, but here is a quick recap below:

- The Fed announced that they are pausing examination work in community banks for the next 30 days and extending the time to respond to non-critical findings.
- The FDIC released an interagency statement and FAQs on loan modifications.
- The Fed has encouraged the use of the Discount Window as an additional liquidity management tool.
- The Fed also encouraged the use of capital and liquidity buffers as they lend to households and businesses affected by the coronavirus.
- The Fed also announced multiple new credit facilities to support the banking industry.

Furthermore, Congress recently passed the CARES Act, which contains multiple banking-specific provisions, such as Troubled Debt Restructuring (TDR) relief, the Payment Protection Program (PPP) through the SBA, and temporarily lowering the Community Bank Leverage Ratio to 8% for capital compliance.

An institution's liquidity model is typically comprised of projections of sources and uses of liquidity, and normally applies stress factors to those projections. It would be prudent to revisit the liquidity projection assumptions first. Primary and secondary sources and uses may change. Some examples of primary sources include performing loan repayments and time deposit rollover rate, while primary uses include loan funding commitments. Wholesale deposits are an example of a secondary source and increases in LOC lines would be a secondary use.

Also, make sure to stress your liquidity projections to evaluate adverse and severe scenarios. Examples of stress scenarios that should be re-evaluated under COVID-19 include:

- Potential of an additional increase in unfunded commitments
- Potential of an additional increase in non-accrual loans
- Potential of a loss of availability of wholesale and jumbo deposits
- Potential of cuts in either secured and unsecured lines of credit
- Potential of further reduction in interest rates

As a final measure, you may need to evaluate your present liquidity policies to determine if they are adequate under the crisis. Board action may be required.

We realize that financial institutions have their hands full these days. So, we hope that we have provided some helpful information or reminders to assist you with all that you are doing. For additional coronavirus information, please visit our COVID-19 Resource Center.

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