



Sight vs. Vision: Preparing Your Balance Sheet for the Future

Financial Institutions Summit



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How Did We Get Here?



Current Themes

- What we know now post SVB, Signature Bank, and First Republic Bank
- What could be expected from examiners
- Hedging and upgraded ALCO meetings are in the spotlight
- Asset/liability sensitivity is irrelevant
- Balance sheet changes matter most
- The typical cycle: Rates * earnings * Liquidity * credit
- The rest of the bond world has lost 85bps of curve in the past 12 months, but most depositories have lost 240bps!
- Are we shrinking or growing this year?
- Loss trades are (still) here, but the motivation and perception has changed

Yield Curve Risk vs. Interest Rate Risk

Index	3/31/22	6/30/22	9/30/22	12/30/22	3/31/23	6/30/23	8/28/23
Fed Funds Target	0.50%	1.75%	3.25%	4.50%	5.00%	5.25%	5.50%
2 Year Treasury	2.33%	2.95%	4.28%	4.43%	4.03%	4.90%	5.05%
3 Year Treasury	2.51%	3.01%	4.29%	4.22%	3.79%	4.53%	4.70%
5 Year Treasury	2.46%	3.04%	4.09%	4.00%	3.57%	4.16%	4.40%
7 Year Treasury	2.43%	3.07%	3.98%	3.97%	3.53%	3.99%	4.32%
10 Year Treasury	2.34%	3.01%	3.83%	3.87%	3.47%	3.84%	4.20%
2-10Yr Treasury Spread	0.01%	0.06%	-0.45%	-0.56%	-0.56%	-1.06%	-0.85%
FFT-5Yr Treasury Spread	1.96%	1.29%	0.84%	-0.50%	-1.43%	-1.09%	-1.10%

Actionable Thoughts

- Stop using beta tied to the fed funds rate – you pay **WHEN** you need it
- Underwrite your deposits: Loyalty vs. trust
- Very few contractual liabilities – optionality risk everywhere
- EVE review
- Unrealized loss from AOCI <15% of total equity / leverage ratio >8% / liquidity ratio >20%
- Marketing / social media: New peer group
- Quantifying what rate movement is necessary to reduce TCE to zero
- Quantifying impact to regulatory capital ratios from selling all bonds or if AFS will be included in reg cap
- Loss trades: Purpose, transparency, and simplicity
- Derivative use – know the difference between **ADVICE & TRADING**
- Derivative education and policy review at the board

Actionable Strategies

- **Mortgage portfolio too long?**
 - Swap low coupon mortgages to floating
- **Hedge future issuance of funding**
 - Enter into forward starting pay fix swap
- **Floors – please don't embed them**
 - Purchase floors from a dealer
- **Loss trades: the how and the why**
 - Remove inefficient leverage soaking up capital on your balance sheet
- **Educate your board and ALCO on the NEXT exposure, not the last!**
 - Where is the next pain for the balance sheet

Plan Your Actions – Take Action on Your Plans

- Strategy development is easy – Execution **SHOULD** be easy
- Communication is often the issue in ALCO / Board
- Focus less on the strategy and more on the logic behind the strategy
- Strategy needs to be actionable:
 - Start doing, stop doing or do differently
- The strategy is not the reason they say no
- Create one page showing execution and its impact on **KEY** metrics

Key Takeaways

- **More capital & stronger liquidity = opportunity to weaponize ALCO (oh, and pressure on earnings)**
- **Start with defining the difference between Tactics & Strategy**
- **Asset and liability sensitivity is irrelevant**
- **You can't predict but you can prepare**
- **Balance sheet moves matter most**
- **Which part or parts of the yield curve matter most to you**
- **Use economic data for pricing, not strategy development**
- **Messaging matters: Purpose, transparency and simplicity**
- **Translate the impact on metrics that matter to the audience**
- **Good CFO's never hear NO at the board, great ones always do!**
- **Play Monday morning QB to educate**

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Scott Hildenbrand is a managing director and the head of the financial strategies group at Piper Sandler. Hildenbrand also runs Piper Sandler Hedging Services, LLC, which is registered as a swap introducing broker with the Commodity Futures Trading Commission and is a member of the National Futures Association.

Previously, Hildenbrand was a principal and chief balance sheet strategist of Sandler O'Neill + Partners, L.P. He headed the balance sheet analysis and strategy group, working with financial institutions on balance sheet strategy development, which includes interest rate risk management, investment portfolio strategy, retail and wholesale funding management, capital planning, budgeting, and stress testing. Hildenbrand also worked closely with the firm's investment banking group to identify and develop strategic opportunities for clients involved in mergers and acquisitions.

Hildenbrand previously worked in Sandler O'Neill's interest rate products group, focusing on developing and implementing structured wholesale funding strategies for financial institutions. He spent his first four years at the firm in the asset/liability management group. Prior to joining Sandler O'Neill in 2004, Hildenbrand worked as a financial analyst in asset/liability management at Tower Federal Credit Union in Maryland.

In 2021 Hildenbrand was elected to the Financial Managers Society board of directors. Additionally, he serves as treasurer on the board of directors for Liam's Room, a non-profit organization that focuses on pediatric palliative care, a specialized approach to medical care for children with serious illnesses.

Hildenbrand holds a Master of Business Administration degree in finance from Loyola College in Maryland and a bachelor's degree with a concentration in accounting and finance from Gettysburg College. He is a frequent speaker at industry conferences and seminars.

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