ASSET/LIABILITY MANAGEMENT – YEAR 1

SECTION LEADER: DWIGHT LARSEN

DESCRIPTION
The Introduction to Asset Liability Management (“ALM”) section builds on the principles learned in the Bank Performance Analysis and Economics and Money Markets sections by reviewing and understanding the primary risks inherent in the bank’s assets and liabilities.

Before getting into the “nuts and bolts of ALM,” it’s worth reiterating that protecting and growing capital is paramount in banking. If capital disappears, the bank disappears! A bank’s capital must support all of the different risks (credit, liquidity, interest rate, operational, etc.) facing the institution as well as providing a base for growth. Maintaining a level of capital that meets regulatory minimums and the risk profile of the bank requires ongoing monitoring and planning. Prudent ALM is a big part of maintaining adequate capital for your bank.

The presentations in this section include an overview of asset liability management and its four main subcomponents; interest rate risk, investment portfolio management, capital management, and liquidity/funding management.

Topics covered in this course include:
- why effective asset/liability management is important in running a successful banking operation
- the structure and function of an effective asset/liability committee (ALCO)
- the various purposes of the investment portfolio and the risks/rewards of various bank investment securities
- tactics and best practices to better manage the bank’s existing and future liquidity needs, including an overview of funding alternatives
- introducing the concept of interest rate risk (IRR), and discussing tools to monitor and manage IRR
- the concept of duration, and how it is used in monitoring interest rate risk
- the importance of managing and maintaining capital

PURPOSE
The purpose of this course is to stress the importance of prudent balance sheet management practices and strategies, since these directly impact earnings and capital. Students will have the opportunity to expand their knowledge of asset liability issues while working on the case studies during the last presentation.

OBJECTIVES
After successfully completing this course, students will be able to understand:
- the purpose and responsibilities of an effective asset/liability committee (ALCO)
- the primary purposes of the bank’s investment portfolio
- the types of securities commonly found in the bank’s investment portfolio and their respective risk/reward characteristics
- the basics of liquidity management, including the need to plan for future liquidity needs (or determine excesses), using projected sources and uses of funding reports
- understanding funding alternatives to a bank’s normal deposit base
- the basics of interest rate risk management, and some of the tools banks use to monitor/manage these risks (i.e., GAP, duration analysis, income simulation, EVE, etc.)
- the impact of changes in market interest rates on the value of loans and investments, and “generally” understand terms such as duration
- why an adequate capital plan is so important in running a successful bank