

# Case Study: Deposit Pricing Strategies to Lower Cost of Funds

September 2020



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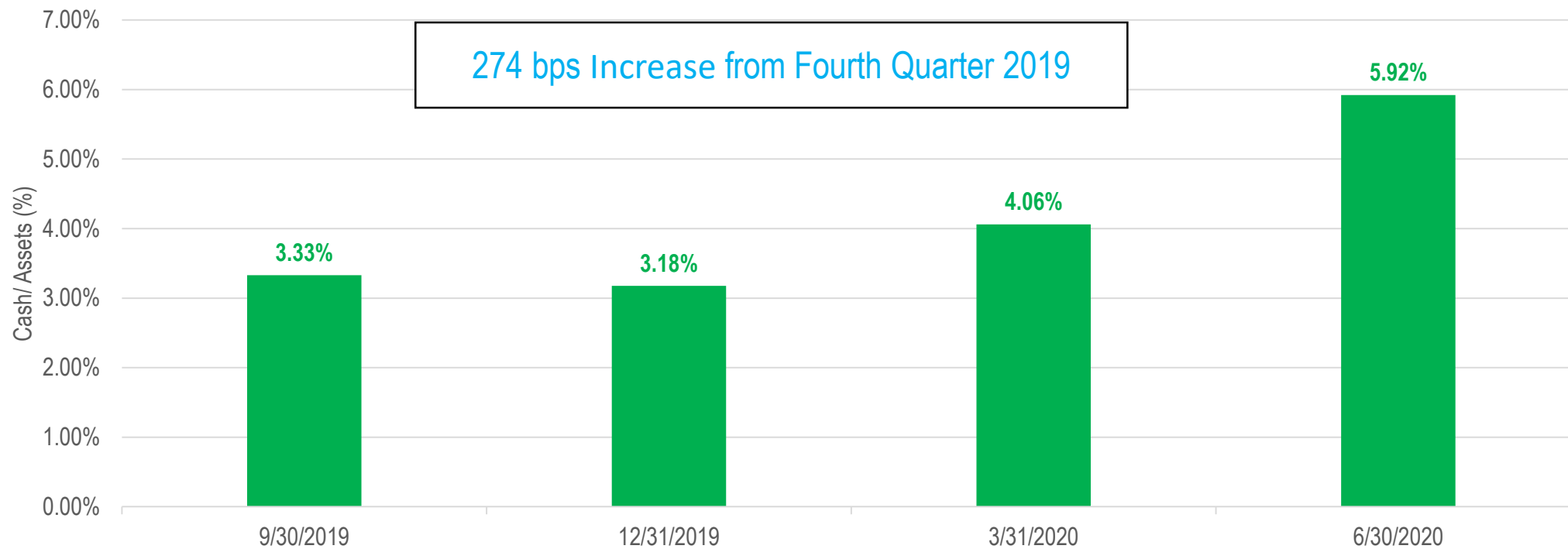
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# Opportunity: Reduce Interest Expense

- Increase in cash poses challenges and opportunities
- Protect margins and optimize cash levels
- FHLBank Boston advances can guide decision making

# Cash Build

Cash/Assets (%) for FHLBank Boston Depository Members

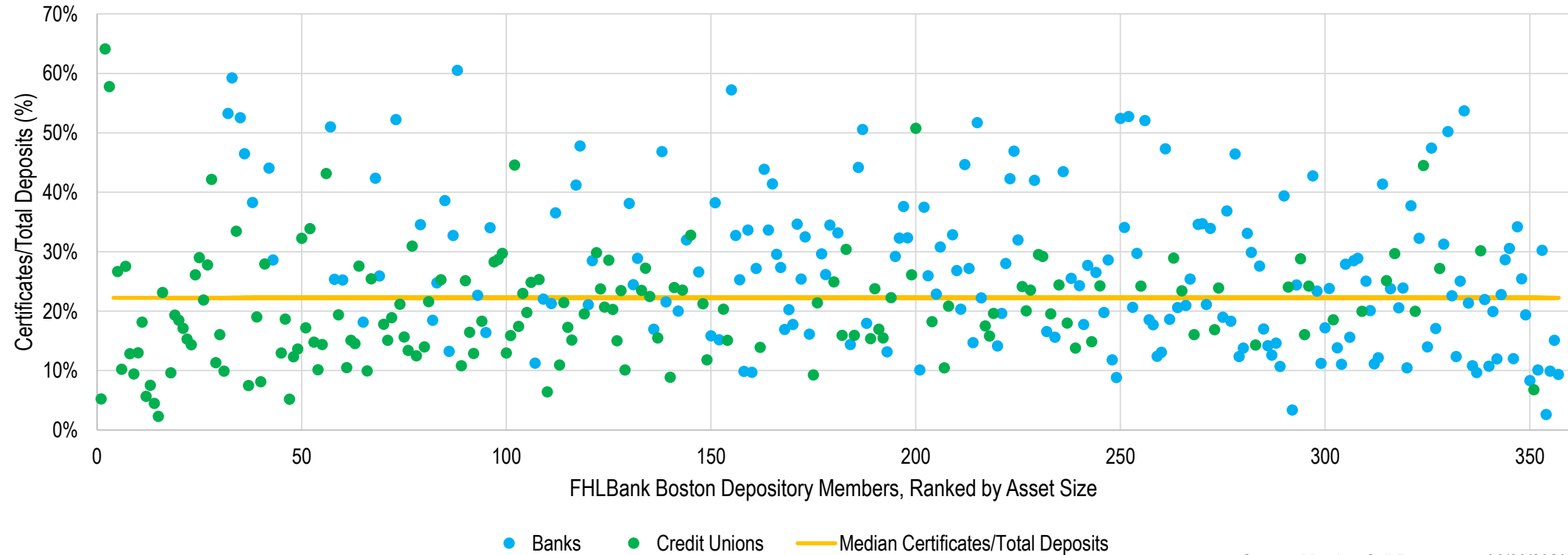


Source: Member Call Reports

- Flight to quality has left many institutions with large cash balances
- Pressure on Net Interest Margin (NIM) increases

# Reliance on Certificate of Deposits (CDs)

CDs/Total Deposits for FHLBank Depository Members



Source: Member Call Reports as of 6/30/2020

- Despite increased cash levels, CD reliance remains high
- **Where should CDs be priced in a 0% rate and high liquidity environment?**

# Input Review: Institution Specific Inputs

## INSTITUTION INPUTS

Total Loans	\$90,000,000	Current Loan/Deposit	94.74%
Total Assets	\$110,000,000	Current Capital Ratio	9.09%
Total Deposits	\$95,000,000	Loan/Deposit Max Limit	105.00%
Total Liabilities	\$100,000,000	Amount of Excess Cash	\$2,500,000
Total Capital	\$10,000,000		

### Overview:

This model assesses the impact to cost of funds and the Loan/Deposit ratio from adjusting deposit rates. You can input the existing amount and current cost for a pool of deposits, as well as assumptions for the amount of deposits you'd expect to retain at various new rates.

As deposits leave the institution, the funding is replaced with advances at a term of your choosing. If your institution is currently experiencing high deposit growth and you would like to runoff balances, you can input the amount of excess cash that would not be replaced by advances.

### Questions to ask:

- What is your current position and where do you want to be?
- With significant deposit growth and slower loan growth, how much room do you have until your internal Loan/Deposit limit is reached?
- With future uncertainty, how much excess cash do you want to hold vs. how much do you want to runoff?

Source: FHLBank Boston

# Input Review: Liability Assumptions

## LIABILITY ASSUMPTIONS

Product Repricing	Liabilities Today		Updated Rates	
	Amount Repricing	Current Weighted Average Rate	Low Offer	High Offer
12-Month Certificates	\$15,000,000	1.50%	0.10%	0.50%
Deposit Retention Rate			30%	80%
	Term (m)	Rate		
Replace Runoff with FHLBank Boston Classic Advances	12	0.37%		

### Assumptions:

This model allows you to input a pool of maturing CDs or you can view a pool of non-maturing deposits where pricing can be adjusted.

The low and high offer can be used to input a range of potential new offer rates. The model looks at all rates in between to assess the financial impact. The retention rate can be used to simulate the impact of rate stickiness based on your depositor tendencies.

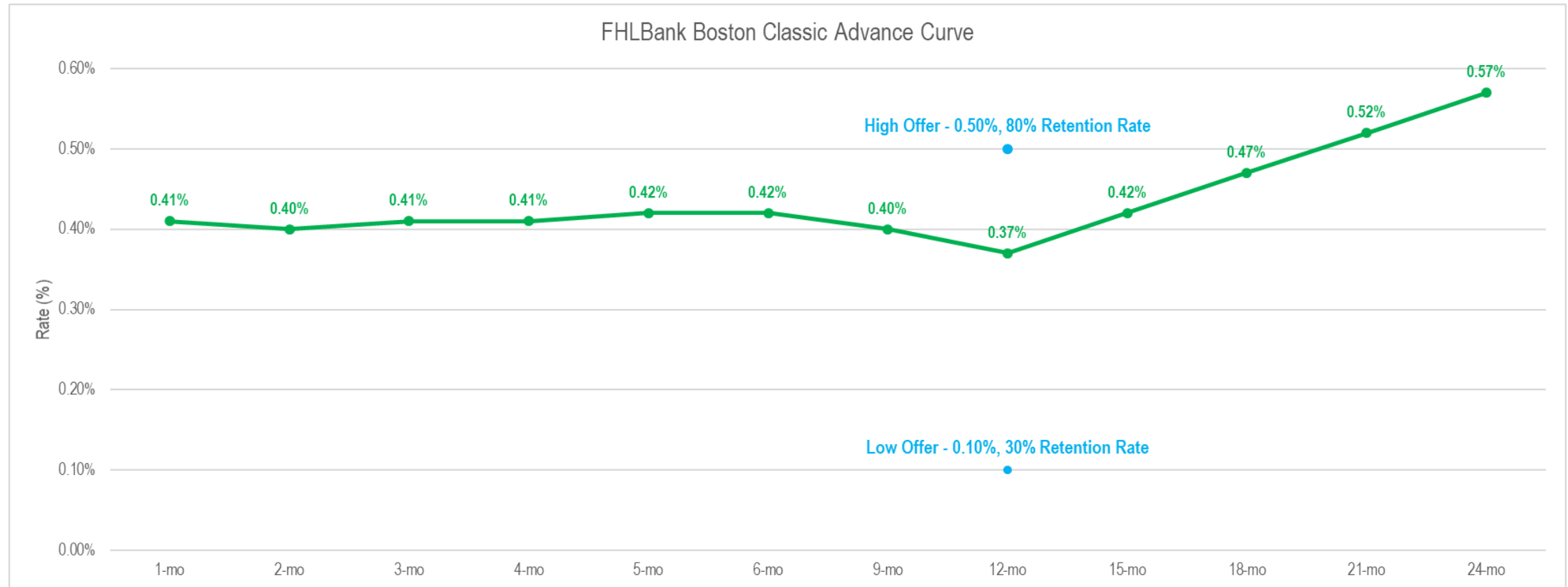
Runoff is replaced with FHLBank Boston Classic Advances unless you choose to input an amount of excess cash that you'd like to runoff. You can select the term that fits your institution's needs.

### Questions to ask:

- Where are you currently pricing?
- Determine range of offer rates and stress test retention ratios based on your own institution's needs as well as customer tendency

Source: FHLBank Boston

# Input Review: Liability Assumptions

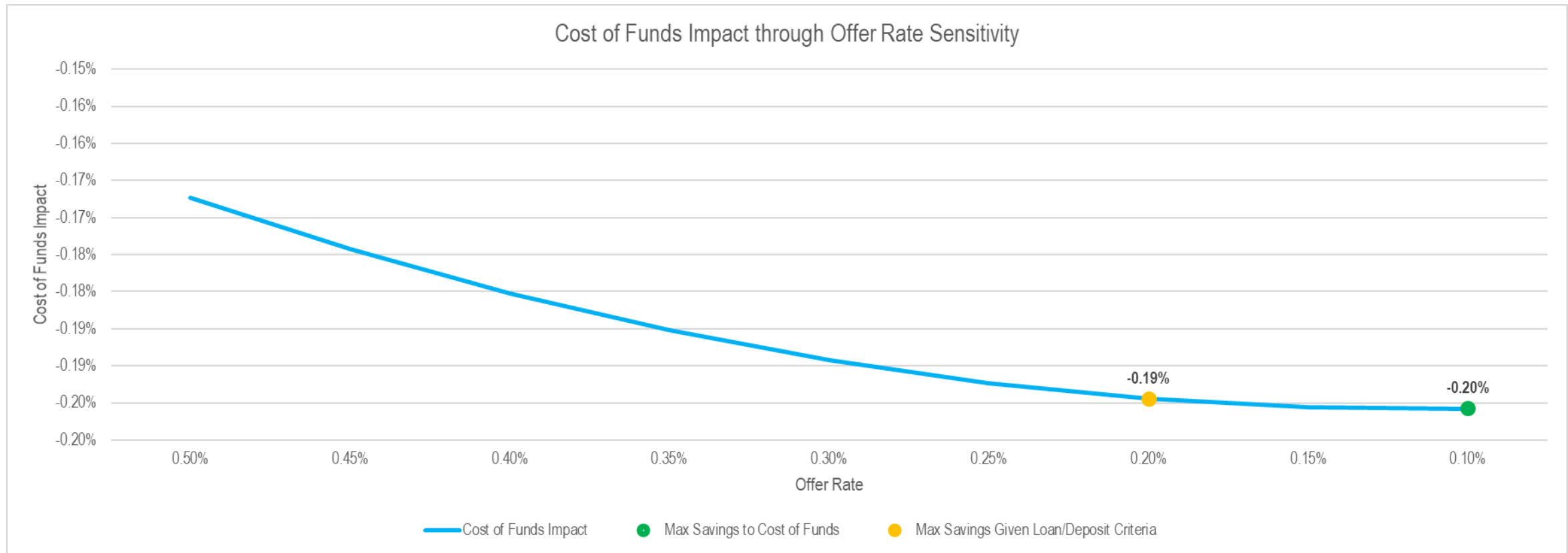


Source: FHLBank Boston

- Utilize FHLBank Boston curve as a guide to pricing
- Fewer and fewer reasons to price above advance curve



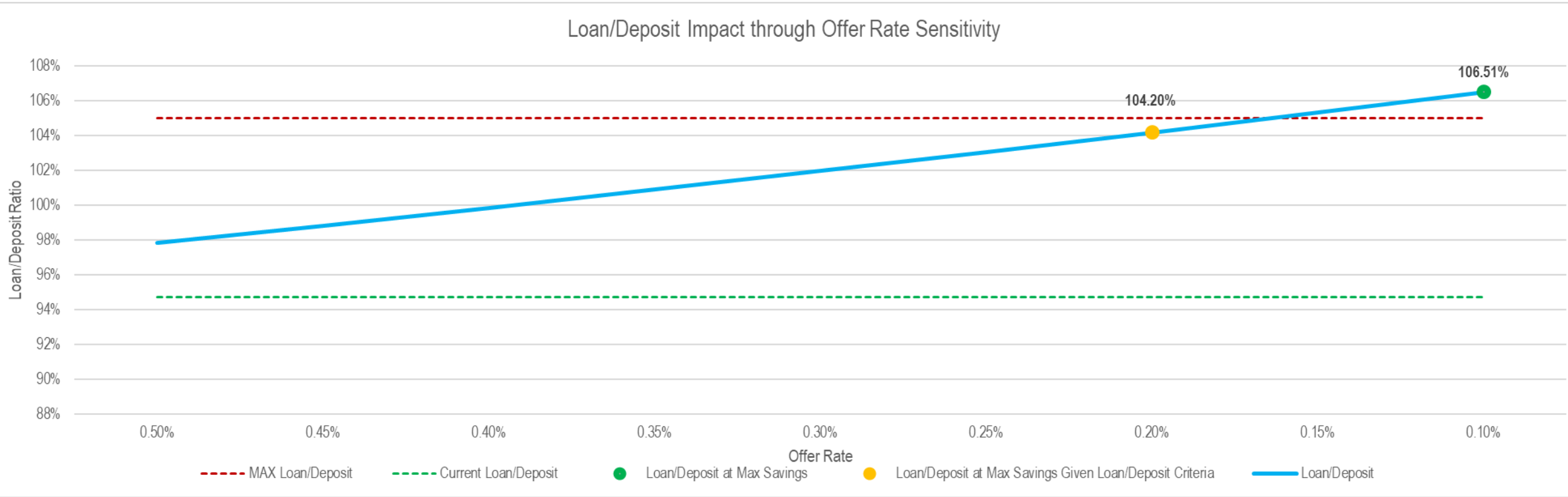
# Output Review: Maximize Cost of Funds Savings



Source: FHLBank Boston

- Review savings across offer rate spectrum
- Max Savings vs. Max Savings Given Loan/Deposit Limit
- Are you achieving maximum savings given input constraints?


# Output Review: Maximize Cost of Funds Savings



Source: FHLBank Boston

- Review Loan/Deposit impact across entire offer rate spectrum
- Loan/Deposit Ratio at Max Savings
- Where do you want to be in the next year?

# Output Review: Total Impact

	Deposit Summary		Advance Summary		Assets/Capital Summary						
	Offer Rate (%)	Deposit Retention Rate (%)	New Deposit Balance (\$)	Cost (\$)	Advance Balance (\$)	Cost (\$)	Total Assets (\$)	Capital Ratio (%)	Blended Cost on Repriced Deposits (%)	Cost Savings to Total Liabilities (%)	Loan/Deposit Ratio (%)
High Offer Rate	0.50%	80%	\$12,000,000	\$60,000	\$500,000	\$1,850	\$107,500,000	9.30%	0.49%	-0.17%	97.83%
 <span style="border: 1px solid blue; padding: 2px;">Max Savings Given Loan/Deposit Criteria</span>	0.20%	43%	\$6,375,000	\$12,750	\$6,125,000	\$22,663	\$107,500,000	9.30%	0.28%	-0.19%	104.20%
Low Offer Rate (Max Savings to Cost of Funds)	0.10%	30%	\$4,500,000	\$4,500	\$8,000,000	\$29,600	\$107,500,000	9.30%	0.27%	-0.20%	106.51%

Source: FHLBank Boston

- **Result: Identify the CD rate that produces the most cost of funds savings**
- FHLBank Boston advances can enhance your ability to maximize cost savings while achieving loan/deposit and liquidity goals

# Summary

- **Cost savings during time of increased margin pressure**
  - Strategically price deposits in a 0% rate environment
  - Maximize margin relief
- **FHLBank Boston curve utilized as a pricing guide**
  - Wholesale funding can support cash needs
  - Optimize the rate you pay for deposits

# Thank You

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