

ZOOM VERSION

“HOW BANKS MAKE MONEY” Bank Financial Management 1

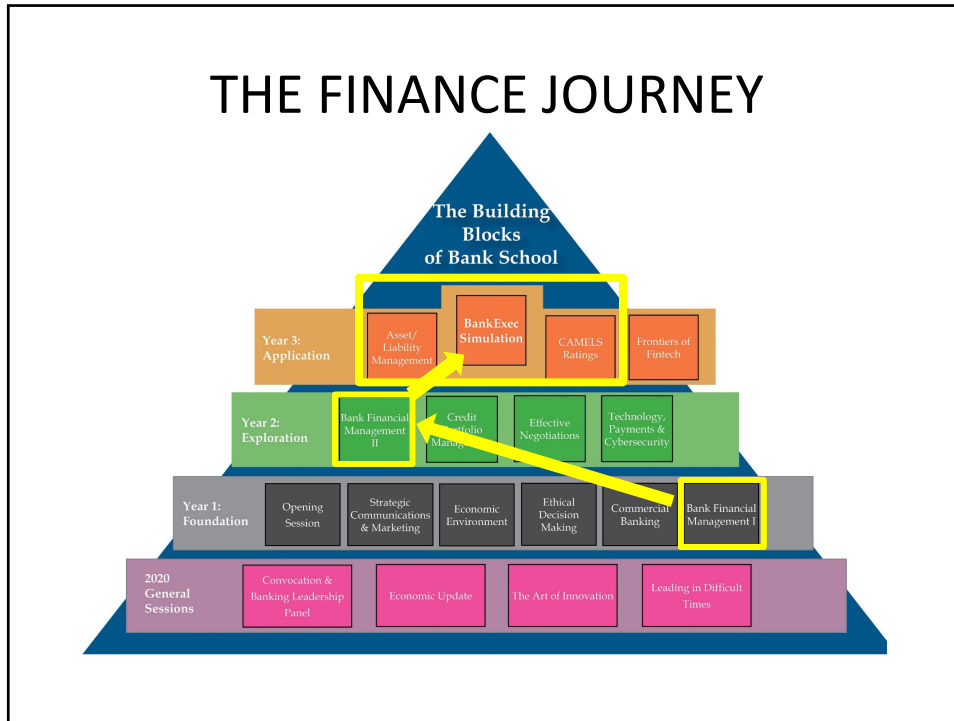
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Goals – Class Overview

- Understand bank balance sheets and how they relate to profitability, liquidity, capital
- Understand bank income statements and how to drive profitability and capital growth
- Understand basic financial ratios/metrics
- Be ready for ALCO Class in year 2
- Make class “virtually” fun!

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Pre-Class Assignment Review

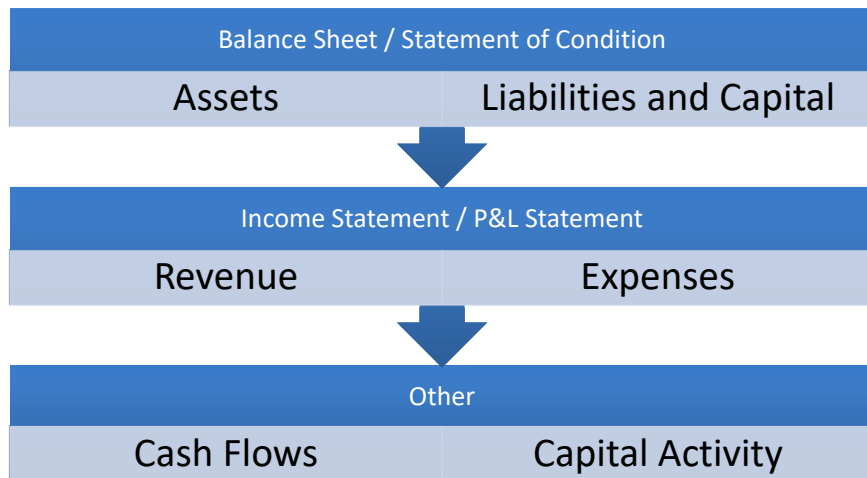
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Why Financial Management?

- Would you play sports without a scoreboard?
- Accounting is the “language of banking”
- Management Tool – Forensic Tool
- Accurate records important to investors regulators, stockholders, directors, management, employees and customers
- Allows you to measure success and compare performance to other banks and overall marketplace
- Used in budgeting and planning

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Bank Financial Statements



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Your Personal Balance Sheet

- Checking Account
- Savings Account
- 401k/Investments
- House
- Car
- Personal Items
- Student Loans
- Car Loan
- Mortgage Loan
- Difference = Net Worth or your personal Capital

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The Balance Sheet “A point in time”

Assets
- Liabilities

Equity/Capital

Why is it called a balance sheet?

WS # 1

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Darden Community Bankshares

Assets	\$ Amount	Liabilities/Capital	\$ Amount
Cash and Due From	\$ 10,000,000	DDA	\$ 200,000,000
Fed Funds Sold	50,000,000	Savings/MMDA	370,000,000
Securities	150,000,000	CDs/IRA Certificates	300,000,000
Loans, Gross	735,000,000	Funds Purchased	0
Reserve Losses	(10,000,000)	Other Borrowings	20,000,000
Fixed Assets	40,000,000	Other Liabilities	10,000,000
OREO	5,000,000	Total Liabilities	900,000,000
Other Assets	20,000,000		
		Equity Capital	100,000,000
Total Assets	\$1,000,000,000	Liabilities & Capital	\$1,000,000,000

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Assets

- Assets are things of value owned by or owed to the company.
- Assets are generally carried at their original cost
 - Exceptions: Investments held for sale
 - Fair Value accounting used in reporting

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Bank Balance Sheet - Assets

- Bank Assets
 - Cash
 - Funds Sold
 - Investments
 - Loans
 - OREO
 - Buildings and Equipment
 - Other Assets
- EARNING ASSETS > 90% TOTAL

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Bank Balance Sheet - Liabilities

- Liabilities are debts or obligations owed by the bank to creditors
- Bank Liabilities
 - Demand Deposits
 - Savings and MMDA
 - Certificates of Deposit
 - Fed Funds/FHLB Funds Purchased
 - Wholesale borrowings
 - Subordinated Debt
 - Other Liabilities

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Bank Capital

- **Assets – Liabilities = Capital**
- **Basic Bank Capital**
 - Common Stock/APIC
 - Retained Earnings
 - +/- Unrealized gains or losses
- **Other forms of Capital**
 - Subordinated Debt
 - Preferred Stock

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Our Focus Areas – Balance Sheet

- +Loans
 - +Allowance for Loan Losses
- +Investments
- +Deposits and other Funding
- +Capital

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Loans Types

- Commercial and Industrial
- Real Estate Secured Loans
 - 1-4 Family
 - Multi-Family
 - Home Equity lines/loans
 - Construction and Development
 - Commercial Real Estate – OO and NOO
- Consumer loans
- Credit card loans
- Overdrawn deposits

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Loans and Leases

- Key issues related to loan portfolios?
 - Asset (Credit) quality
 - Risk Ratings Systems
 - Allowance for Loan and Lease Losses / CECL
 - Interest rate risk
 - Fixed rates, duration analysis
 - Floating rates, indexes, floors, hedging
 - Concentration of credit
 - Mix of Loan Types
 - Sector 100/300 Ratios
 - Legal lending limits/House lending limits

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Darden Community Bankshares

Assets	\$ Amount	Liabilities/Capital	\$ Amount
Cash and Due From	\$ 10,000,000	DDA	\$ 200,000,000
Fed Funds Sold	50,000,000	Commercial and Industrial	\$150,000,000
Securities	150,000,000	Commercial RE – OO	\$100,000,000
Loans, Gross	735,000,000	Commercial RE - NOO	\$175,000,000
Reserve Losses	(10,000,000)	Construction & Development	\$75,000,000
Fixed Assets	40,000,000	1-4 Family Residential	\$200,000,000
OREO	5,000,000	Consumer Loans	<u>\$35,000,000</u>
Other Assets	20,000,000	Gross `Loans	<u>\$735,000,000</u>
		Equity Capital	100,000,000
Total Assets	\$1,000,000,000	Liabilities & Capital	\$1,000,000,000

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Ratio: Loan to Deposit Ratio

- Is a very simplistic liquidity measurement
- Demonstrates the level of deposits funding the loan portfolio
- A ratio too high (90-100%+) may impact liquidity but will lead to higher profitability
- A ratio too low also requires some attention and may have a negative impact on profitability
- Calculation:
 - Total Loans / Total Deposits
 - \$_____/ \$_____ =

WS # 2