2026 Oklahoma Seminar

DAY 2

The BakerGroup

Welcome

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Regulatory Updates and Survey Responses

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New Laws & Regulations: Already Up & Running

Jul 2026

21st Century ROAD to Housing Act

Aimed to address housing needs and accessibility. Added some meaningful changes to banking codes and regulation.

Jul 2026

Community Bank Leverage Ratio

Adjusted down to 8% Tier 1 Leverage for Community Banks. Extended grace periods.

Aug 2026

Safety and Soundness Regulatory Definition

First actual definition for what constitutes Safety & Soundness.

Aug 2026

Regulatory Concern Approaches

Most clear outline of when most regulators will take meaningful steps to address MRAs and Technical Violations. Closely tied to the official definition for S&S practices.

GENIUS Act Updates

What is this Act?

The **G**uiding and **E**stablishing **N**ational **I**nnovation for **U**.S. **S**tablecoins **Act** establishes the licensing system to allow entities to issue stablecoin, pegged to the U.S. dollar. Disallows any bank with FDIC coverage from being an issuer. Must be a bank subsidiary, or fully independent.

What is US Payment Stablecoin?

Four tests to meet definition:

1. Is SOLELY a Digital Asset.
2. Is used only as source of payment/settlement of debt.
3. Is fixed in value to a fiat currency (can be foreign currency).
4. Is reasonably expected to maintain stable value.

Who has authority to issue licenses?

Essentially, every federal bank regulator. Even the state level licensing is backstopped by the Federal Reserve Bank. FinCEN treats all issuers as financial institutions for BSA coverage. The U.S. Treasury has oversight of each regulator, and any foreign issuers.

Timeline So Far

Jul 2025 — Law signed by President in July 2025.

2026 — Each Federal Bank Regulator has independently asked for comment on proposals.

*There's enough difference in each that multiple Bank Advocacy Groups sent joint letter asking for conformity in rules.

Sep 2026 — The FDIC recently closed comment period. No notice of when response expected.

Sep 2026 — The U.S. Treasury issued an "Interim Final Rule" Sept 30. Established the state-certification process. Awaiting review of forms before applications may be accepted.

Nov 2026 — OCC expects their final rule to be issued in Nov of this year.

Nov 2026 — The Federal Reserve has a comment period open until Nov 28, 2026, for two proposals related to the (1) application process, as well as (2) capital and risk standards and anti-tying rules.

Jan 2027 — Takes effect in January 2027, or when final rules issued, whichever is sooner.

CRA Updates

There were major changes to CRA, which were reverted back to 1995 rules. New rules currently proposed, but no firm date for enaction set. FRB has not issued any new rules.

Jul 2025 The joint final rules for CRA in 2023 were rescinded in July 2025, by a joint notice of rule making.

Jul 2026 Now, the OCC and the FDIC have gone ahead with changes, without the Federal Reserve joining in.

Oct 2026 The window for public comment closed Oct 13, and the final rule is in process of being released.

Pending The Federal Reserve has yet to issue a proposal for changes to CRA, at least as of writing this slide.

Major Updates from Proposed Rules

- Asset Thresholds Raised – Kept the language for annual increases tied to inflation. Proposed increase is well beyond inflation.
- Lending and Service Tests Changed – Limits testing to four categories, with only two categories allowed per examination. No more deposits in service tests, only lending
- Community Development Definitions – More clarity on Community Development overall. ISB Banks no longer need to be Sat in CD Testing to be Sat overall.
- Assessment Areas Unchanged – Unlike last CRA proposal, AAs are unchanged with this new proposal.
- Strategic Plan and Application Process – The proposal updates application processes, and timely feedback.
- Discrimination Determinations – If discrimination is suspected, it would need to be escalated before it hits report.

This change is specific to National and Non-Member State Banks. FRB has not taken part.

Unsafe & Unsound Defined

For the first time, there is a codified definition for what is Unsafe & Unsound. The new outline states:

1. The activity must be contrary to generally accepted standards of prudent banking activities, AND
2. The activity must (i) if continued, materially harms financial condition of the bank or insurance fund, or (ii) has already materially harmed the financial condition of the bank.

Matters Requiring Attention

Now must meet the definition of Unsafe & Unsound to be issued. Still require action be taken by bank.

Supervisory Observation

Concerns that do not elevate to an MRA. Does not require action to be taken by bank, but is a direction for potential risks to develop.

Safety & Soundness Definitions and Supervisory Concern Approaches

This new approach puts more responsibility on the bank's risk management, not just relief.

Bank Failures Since Jan 2023	Number of Banks With Public Enforcement Actions
15	10

Since the first bank failure of 2023 through the second week of October 2026, a third of all banks that have failed or been taken into conservatorship hadn't reach any level of public enforcement actions.

Just because the regulators have provided more concrete definitions and changed their approach to bring risk to Management's attention, does not mean that risk management practices should become lax for your bank.

Asset Quality

- Loan Risk Rating Classifications:
  - Examiners are going to be more tough since interest rates increased after Sep FOMC meeting. Classifying loans in a timely manner is a direct reflection of risk management practices. Being able to justify keeping loans at more favorable risk ratings is going to be more burden for bank.

- Cash Flow Stress Testing:
  - Examiners are going to expect more stress testing on each loan, not just portfolio. As loans begin to reprice, you'll need to know if the customer can still maintain their repayment. That risk should be identified before the loan reprices, and well before a customer misses a payment.

- Underwriting and Collateral Valuations:
  - Loans are going to continue to be arguably the largest risk on a banks balance sheet. Examiners are going to be looking for the little practices that reflect a strong credit quality program.

Liquidity

- On-Balance Sheet Liquidity and Borrowing Capacity:
  - These focus on how liquidity is managed. Are you maintaining investments without extensive depreciation? How much of your loan/investment portfolio is pledged? Do you have a lot of slow-pay loans? Are all of your cash flows from longer term assets?

- Stress Testing and Contingency Funding Plans:
  - There have been significant changes in the financial market over the past six years. Not just interest rates, but accessing lines at the FHLB, Fed, and Correspondent Banks. Processes have been updated. How long will it take you to get funds from your lines? How much of your line depends on stable interest rates?

- Deposit Concentrations and Uninsured Balances:
  - Given the number of financial institutions that have closed over the recent few years, there have been multiple hits to the Deposit Insurance Fund. Examiners are going to be more critical of those balances that aren't covered by FDIC insurance.

CECL, Governance, Capital and Strategic Planning

- Current Expected Credit Losses:
  - This has been widely over complicated. From a very high-level over simplification, this is the previous ALLL method with the added input from management on what the near-term markets will do.

- Governance:
  - The start of the entire risk management framework is governance. A board outlines what they see as acceptable risks, they outline what limits are set by those risks in policies, the policies guide management's procedures, audit affirms those procedures meet the risk limits set in policies. It's all based on the first step being meaningful.

- Capital and Strategic Planning:
  - Capital and Strategic Planning supports the Governance function. It shows that the board and management have taken the time to make informed, supported decisions. It's a refocus for where you want to take your bank, or if you are going to try and coast to accrue earnings for a while.

Regulatory Focus Items

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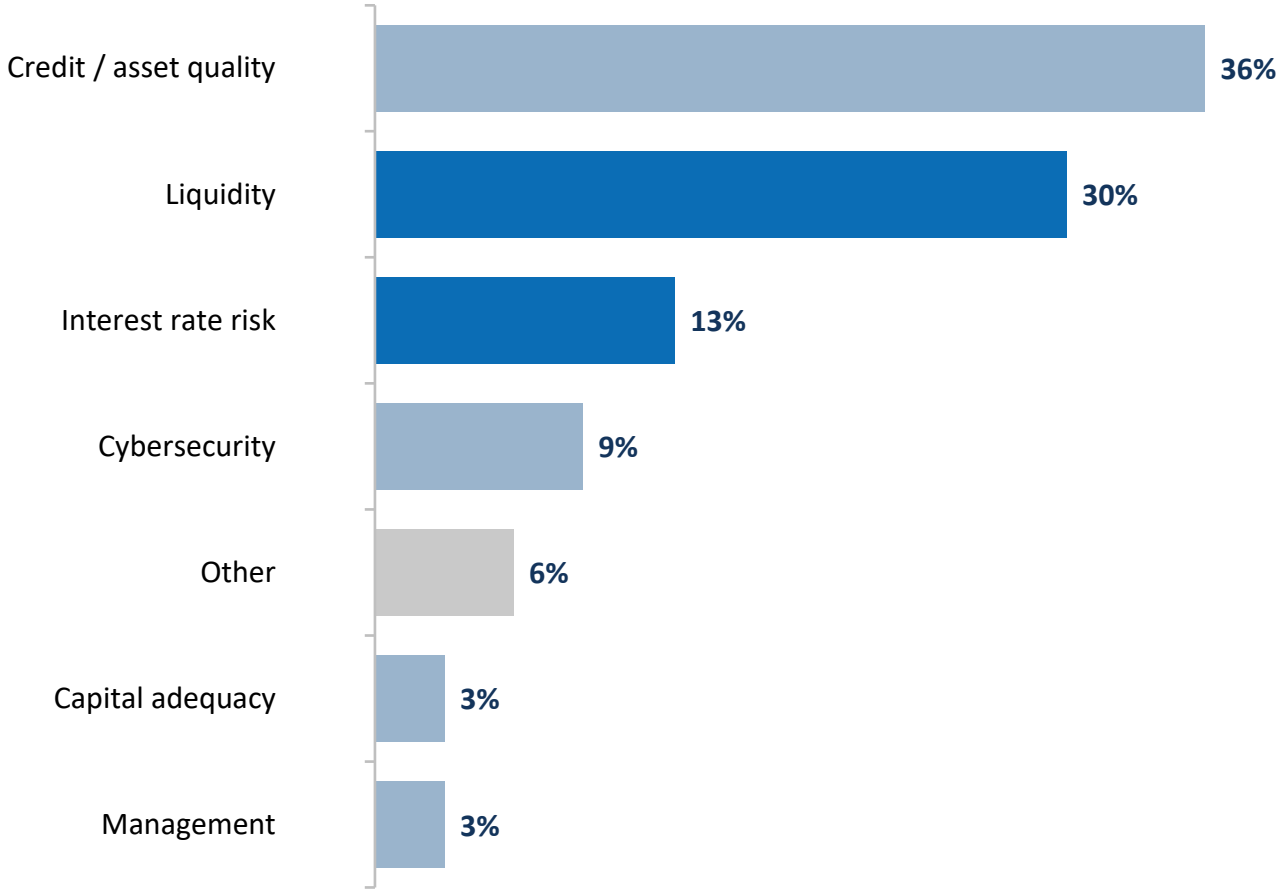
Regulatory Focus Items for 2026

- **Liquidity Risk Management**
  stress testing, contingency funding, deposit concentrations
- **Interest Rate Risk Management**
  assumptions, back-testing, rising-rate scenarios
- **Credit Risk — CRE Refinancing**
  loans originated at low rates maturing into today's rates
- **Agricultural Credit**
  third year of falling row-crop revenue; delinquencies rising
- **Earnings and Funding Costs**
  margins improved; funding costs now turning back up
- **Unrealized Portfolio Losses**
  lowest since 2021 at year-end — but rates have moved since
- **Cybersecurity and Fraud**
  AI-enabled attacks, impersonation scams, payment fraud
- **BSA/AML and Sanctions**
  risk-based programs; geopolitical sanctions exposure
- **AI and Third-Party Risk**
  AI inventory and governance; core-provider oversight

Sources: OCC Semiannual Risk Perspective, Spring 2026; FDIC 2026 Risk Review; Federal Reserve Supervision and Regulation Report (June 2026); The Baker Group's Community Bank Survey, 3Q 2026.

What Examiners Are Asking About

"What was the main focus from the regulators on your last risk management examination?"



43% said Liquidity or IRR

vs. 36% who said credit. That is where this session spends its time.

HOT TOPICS FROM YOUR LAST EXAM (MENTIONS)

- **49** Credit and asset quality
- **46** Liquidity, funding and contingency planning
- **29** Cybersecurity, IT and third-party risk
- **29** Interest rate risk, ALM and margin
- **18** Governance, planning and policy
- **11** AI, crypto and emerging technology

Source: The Baker Group's Community Bank Survey, 3Q 2026 (n ≈ 264). Hot topics are coded open-ended mentions; respondents could name more than one.

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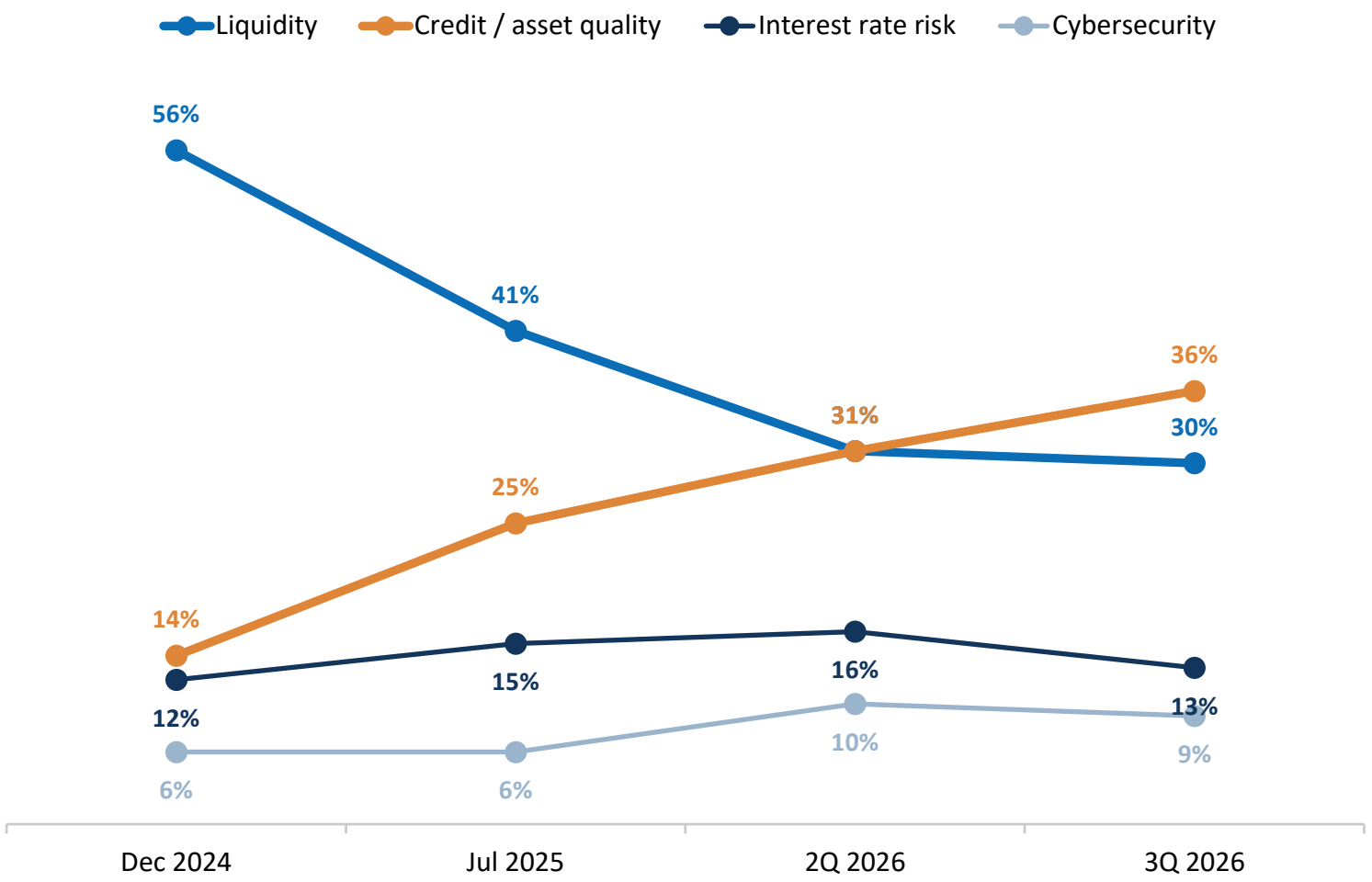
Exam Focus Is Rotating From Liquidity to Credit

"What was the main focus from the regulators on your last risk management examination?" — four Baker surveys, Dec 2024 to 3Q 2026.



THE ROTATION

56% → 30%

Liquidity as the main exam focus, Dec 2024 to 3Q 2026

14% → 36%

Credit and asset quality over the same period

Liquidity hasn't gone away — it's now the expectation. Credit is where the follow-up questions are, especially CRE refinancing and ag.

Source: The Baker Group's Community Bank Survey: Dec 2024 (n = 185), Jul 2025 (n = 255), 2Q 2026 (n = 177), 3Q 2026 (n ≈ 264). Multiple choice; capital, management and other not shown.

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OCC Semiannual Risk Perspective — Spring 2026

The OCC's National Risk Committee view of the federal banking system, data as of December 31, 2025.

EXECUTIVE SUMMARY HIGHLIGHTS

"Balance sheets remain strong, with capital ratios and liquidity high by historical standards."

"Credit risk within the federal banking system remains manageable in aggregate."

"Credit conditions and refinancing risk in certain segments of commercial real estate lending and of private credit markets warrant ongoing monitoring."

"Cyber threats and fraud remain a concern."

"Geopolitical tensions increase sanctions and money laundering risk, straining bank compliance systems."

KEY RISK THEMES

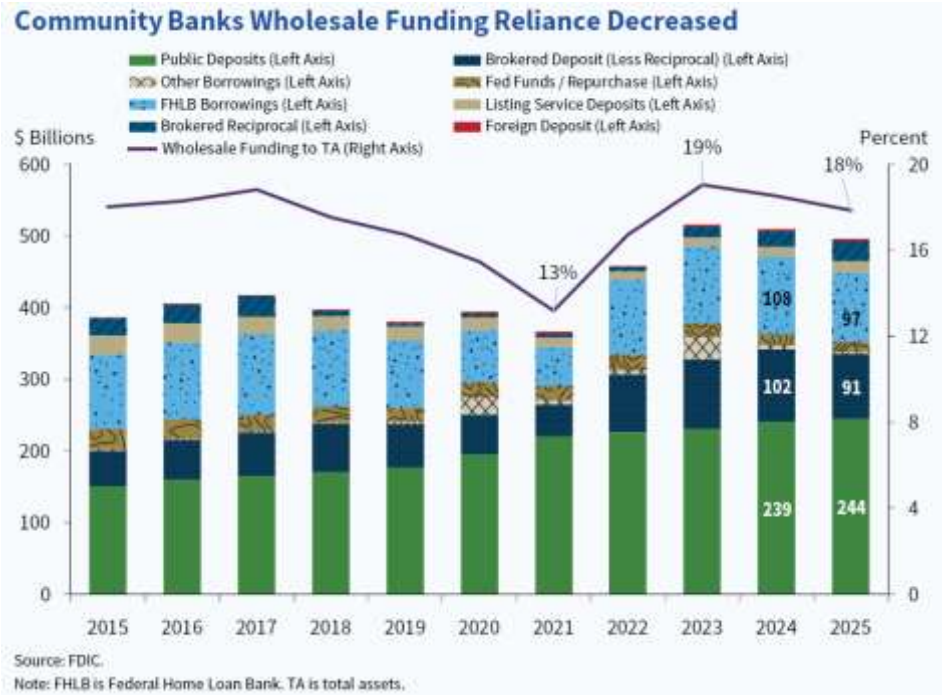
- **Credit:** CRE refinancing; private credit; consumer past dues at weaker borrowers
- **Market:** NIM improved in 2025 on lower funding costs — more at banks under $30B
- **Operational:** cyber, AI-enabled attacks, fraud and scams
- **Compliance:** sanctions and BSA/AML; tailored community bank exam procedures
- **Innovation:** AI governance; GENIUS Act stablecoin rules

Source: OCC Semiannual Risk Perspective, Spring 2026 (released May 7, 2026).

FDIC 2026 Risk Review — Performance, Margin and Funding

Strong 2025 earnings, a margin that kept rising, and community banks leaning less on wholesale funding.





- Industry earnings strong for 2025 on higher interest and noninterest income
- Net interest margins modest but improved as the yield curve steepened
- Problem banks remained in the normal range for non-crisis periods

- On-balance-sheet liquidity stable; banks kept building borrowing capacity
- Deposit growth led by uninsured deposits
- Wholesale funding reliance eased: lower FHLB borrowings and brokered deposits

Source: FDIC, 2026 Risk Review (data through 4Q 2025). Charts reproduced from the FDIC report.

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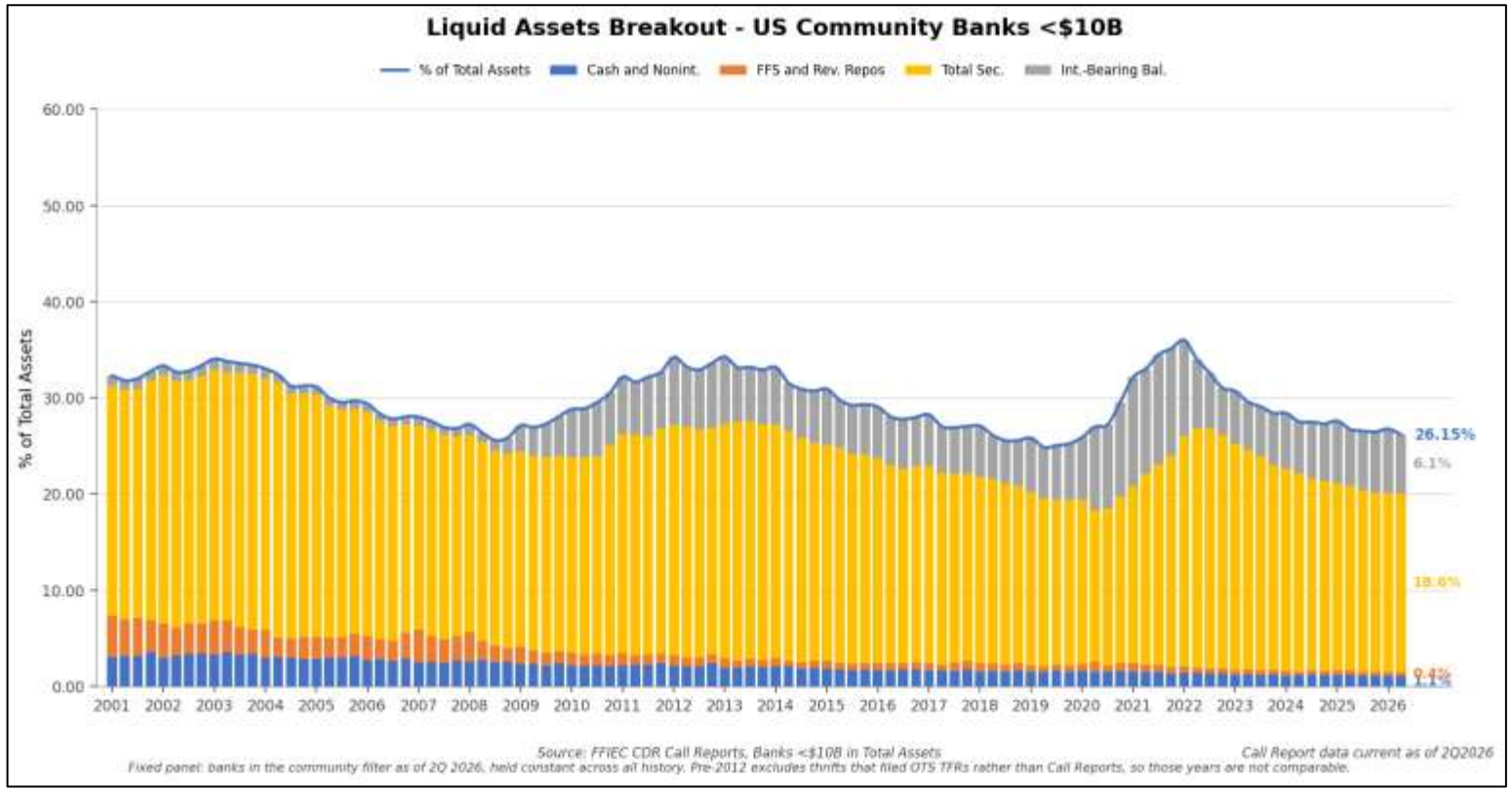
Liquidity Asset Breakdown



26.2%

Liquid assets, % of total assets, 2Q 2026 — down from ~36% at the end of 2021

+$61B vs. +$15B

Small-bank loans vs. deposits since July 1; cash −$22B (Fed H.8)

32% vs. 28%

Of bankers say on-balance-sheet liquidity is increasing vs. decreasing (40% flat); 19% increased wholesale borrowings in the last 90 days

Sources: FFIEC CDR Call Reports, community banks <$10B (fixed panel), through 2Q 2026; Federal Reserve H.8 via FRED (week ending Sep 23, 2026); The Baker Group's Community Bank Survey, 3Q 2026 (n ≈ 264).

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Cyber, Fraud, BSA and Model Risk

The OCC's operational and compliance themes — and the places it is tailoring expectations for community banks.

CYBERSECURITY

- AI lowers the barrier to entry for attackers and speeds up attacks
- Geopolitical tension raises the threat from state-sponsored actors
- Multifactor authentication and timely patching are the named mitigants

FRAUD

- A key driver of operational losses
- Impersonation scams via text and social media
- A dynamic, adaptive approach is warranted; FinCEN alerts on new typologies

BSA / AML

- Sanctions and money-laundering risk rising with geopolitics
- Tailored community bank BSA exam procedures (OCC Bulletin 2025-37)
- Proposed risk-based AML/CFT program rule (Apr 2026)

MODEL RISK

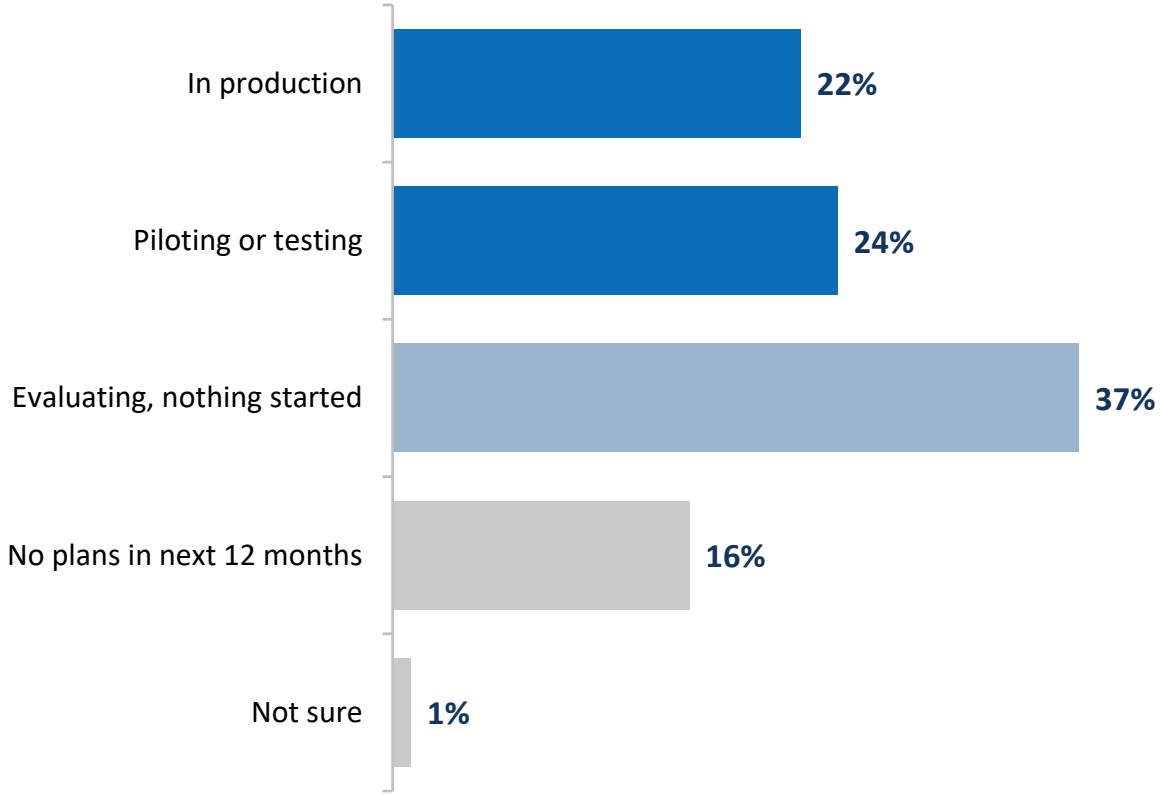
- Revised interagency model risk guidance (Apr 17, 2026)
- Risk-based and commensurate with size, complexity and materiality
- Generative and agentic AI are outside its scope for now

Sources: OCC Semiannual Risk Perspective, Spring 2026; OCC Bulletins 2025-37 and 2026-13; FinCEN/agencies AML/CFT proposal (Apr 7, 2026).

AI: Examiners Want to See an Inventory

Nearly half of you are already piloting or using AI. The supervisory expectation is governance that keeps up.

"IS YOUR BANK CURRENTLY USING AI IN ANY PART OF ITS OPERATIONS?"



WHAT A STATE EXAMINER MAY ASK FOR (CSBS, SEP 2026)

- An inventory of AI tools and use cases
- Governance and board oversight
- Third-party and AI-vendor risk management
- Model risk management and validation
- Consumer protection controls
- Generative and agentic AI, specifically

WHERE YOU GET AI GUIDANCE (MENTIONS)

45 associations · **33** vendors · **25** internal IT · **25** consultants/auditors · **17** no source

Sources: Conference of State Bank Supervisors, AI Supervisory Framework (Sep 16, 2026); The Baker Group's Community Bank Survey, 3Q 2026 (n ≈ 264).

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Today's Liquidity Environment and Best Practices

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The Fed is tightening again

3.75–4%

Fed funds target

Raised 9/16/26; first hike since 2023

5.29%

10-year Treasury (9/30/26)

Highest in roughly two decades

4.1%

FOMC median, fed funds at year-end 2026

Implies one more hike

3.4%

CPI, year over year

August 2026

What higher-for-longer means for liquidity

Deposit competition may pick up

Since July, more than 80% of advertised CD rate changes have been increases, and the Fed's hike may add more pressure.

Bond prices have fallen

The 2-year is up 150bp and the 10-year 132bp since Feb. 27, pushing market values down.

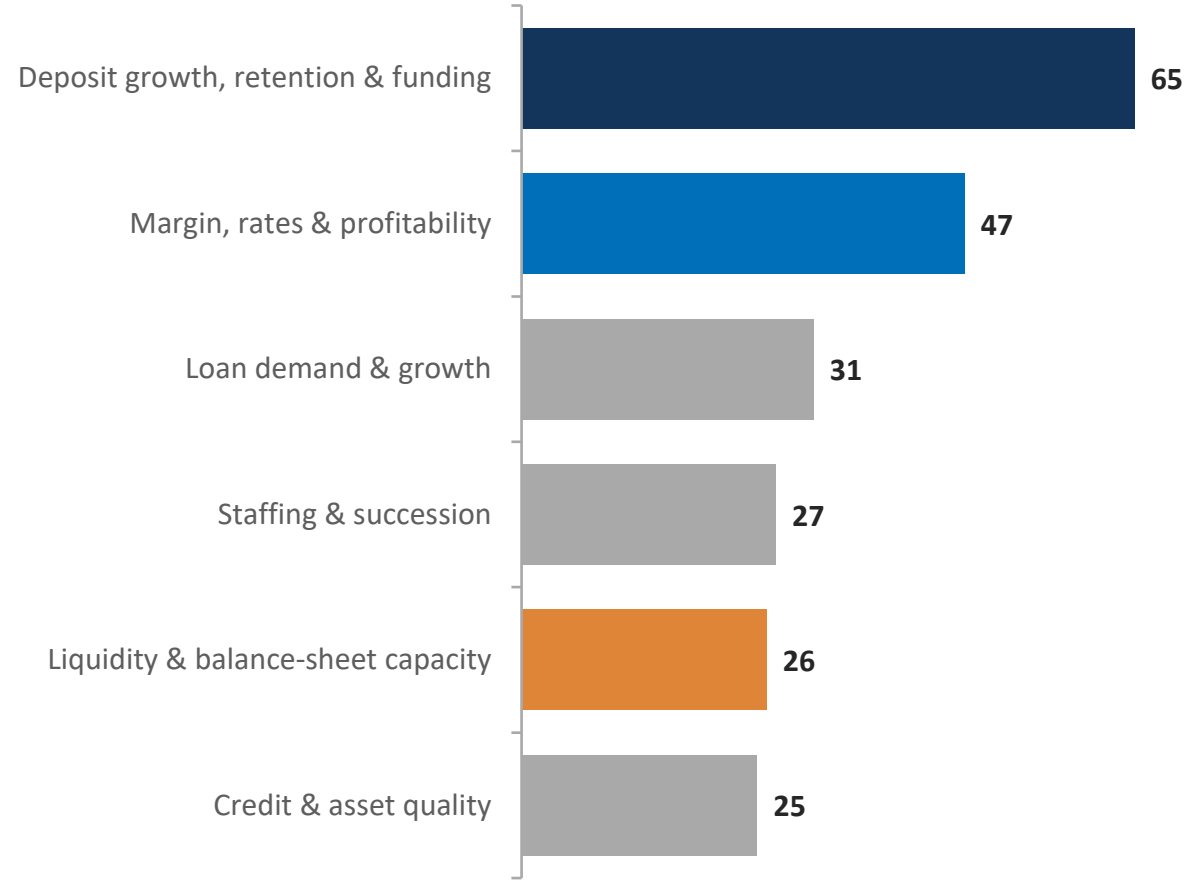
Cash flow could slow

Fewer refinancings mean slower loan and MBS paydowns, so less cash comes back on its own.

Sources: Federal Reserve FOMC statement and Chair's press conference (9/16/26); U.S. Treasury daily par yield curve (9/30/26); BLS CPI (August 2026); CD Valet, September 2026 CD rate trends.

Bankers already see funding as a top challenge

Biggest challenge, next 12 months (mentions; open-ended)



30%

said liquidity was the main focus of their last exam (#2 after credit)

85%

expected cost of funds flat or up 0–25bp, before the hike

Key points

- Deposits and funding are the #1 worry, by a wide margin
- Examiners are asking about liquidity, funding and contingency planning
- Funding-cost expectations were set before the Fed reversed course

Source: The Baker Group Community Bank Survey, 3Q 2026 (n ≈ 264). Survey closed before the 9/16/26 FOMC meeting.

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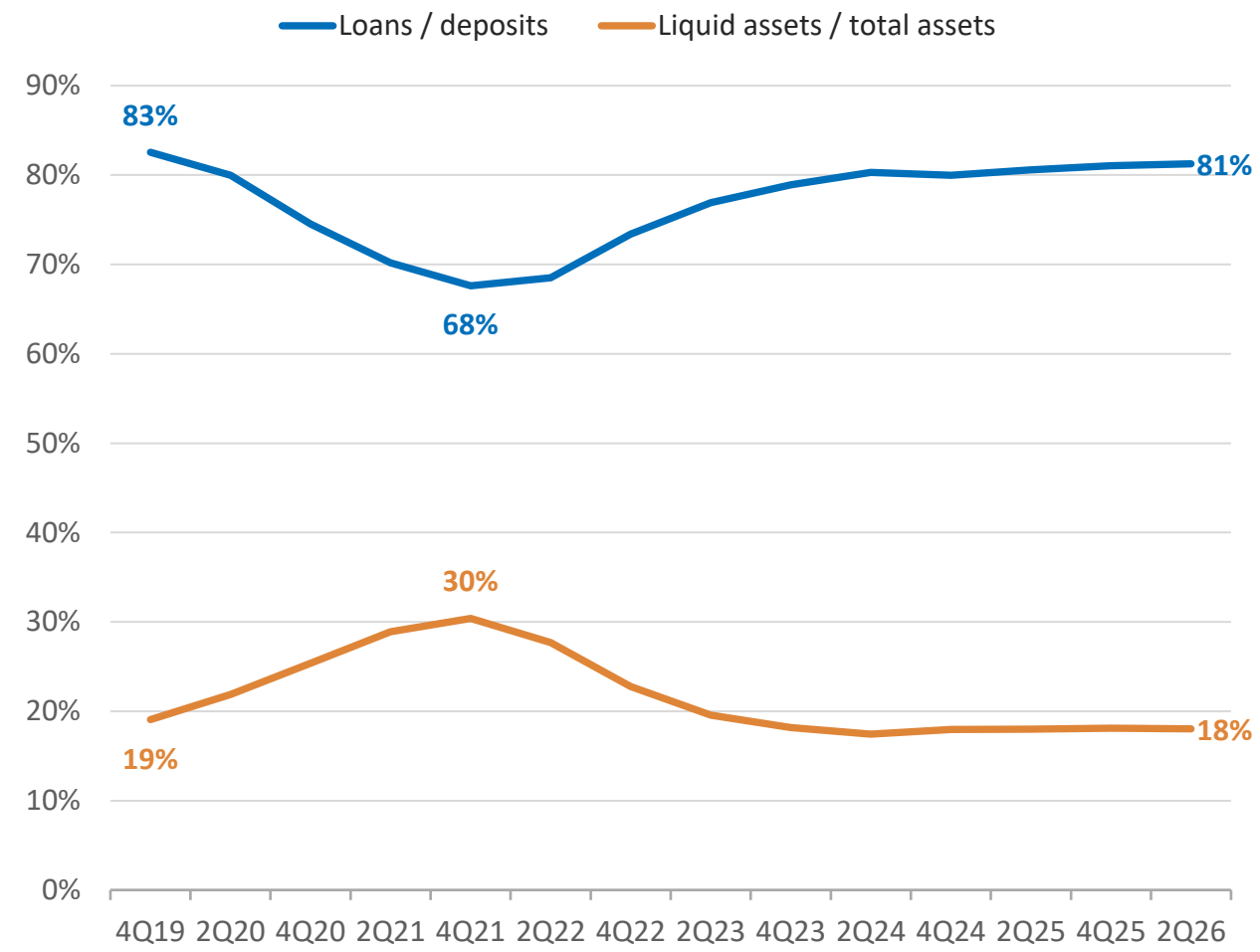
Liquidity tightened, then stayed tight



Source: Call report data via S&P Global; median of U.S. banks under $10B in total assets (4,079 banks at 6/30/26).

68%→81%

Loans / deposits, 4Q21 to 2Q26

30%→18%

Liquid assets / assets, same period

Key points

- Pandemic deposits lifted liquid assets to about 30% of assets in 2021; loans/deposits fell to about 68%
- That excess liquidity is now gone: loans/deposits are back to 81% and liquid assets are about 18%, near 2019 levels
- Liquidity is starting from a tighter point than when the Fed last raised rates

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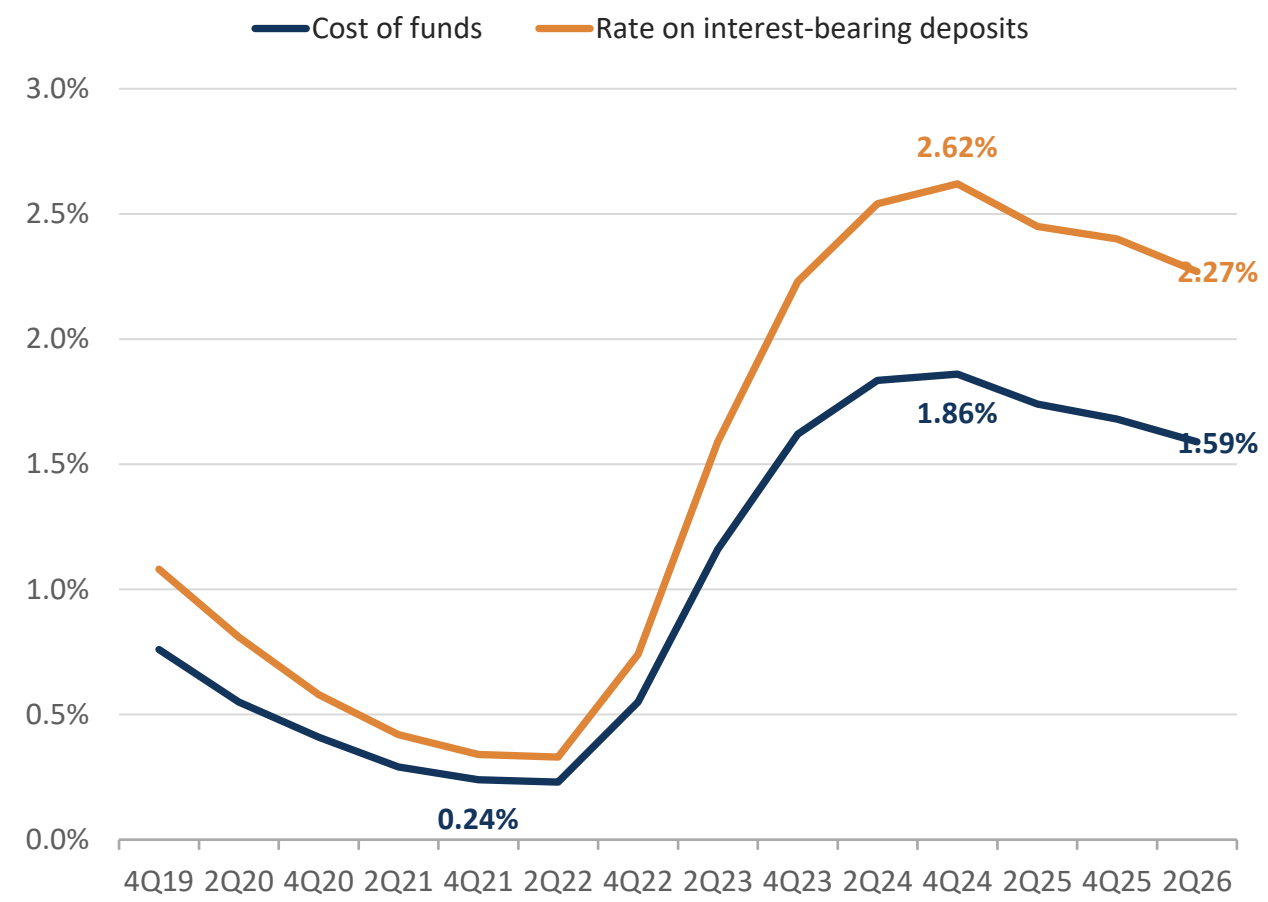
Deposits got more expensive and more rate-sensitive

Median cost of funds and rate on interest-bearing deposits



Source: Call report data via S&P Global; median of U.S. banks under $10B in total assets (4,079 banks at 6/30/26).

19%→30%

Time deposits, share of deposits (4Q21 to 2Q26)

26%→21%

Noninterest-bearing, share of deposits

Key points

- Cost of funds rose from 0.24% at year-end 2021 to 1.86% at year-end 2024, then eased to 1.59% by mid-2026 after the late-2025 cuts
- The bigger story is the mix: CDs grew from 19% to 30% of deposits, and noninterest-bearing fell from 26% to 21%
- A CD-heavy deposit base reprices faster and can be more likely to move for a better rate
- With the Fed hiking again, that easing in cost of funds may reverse

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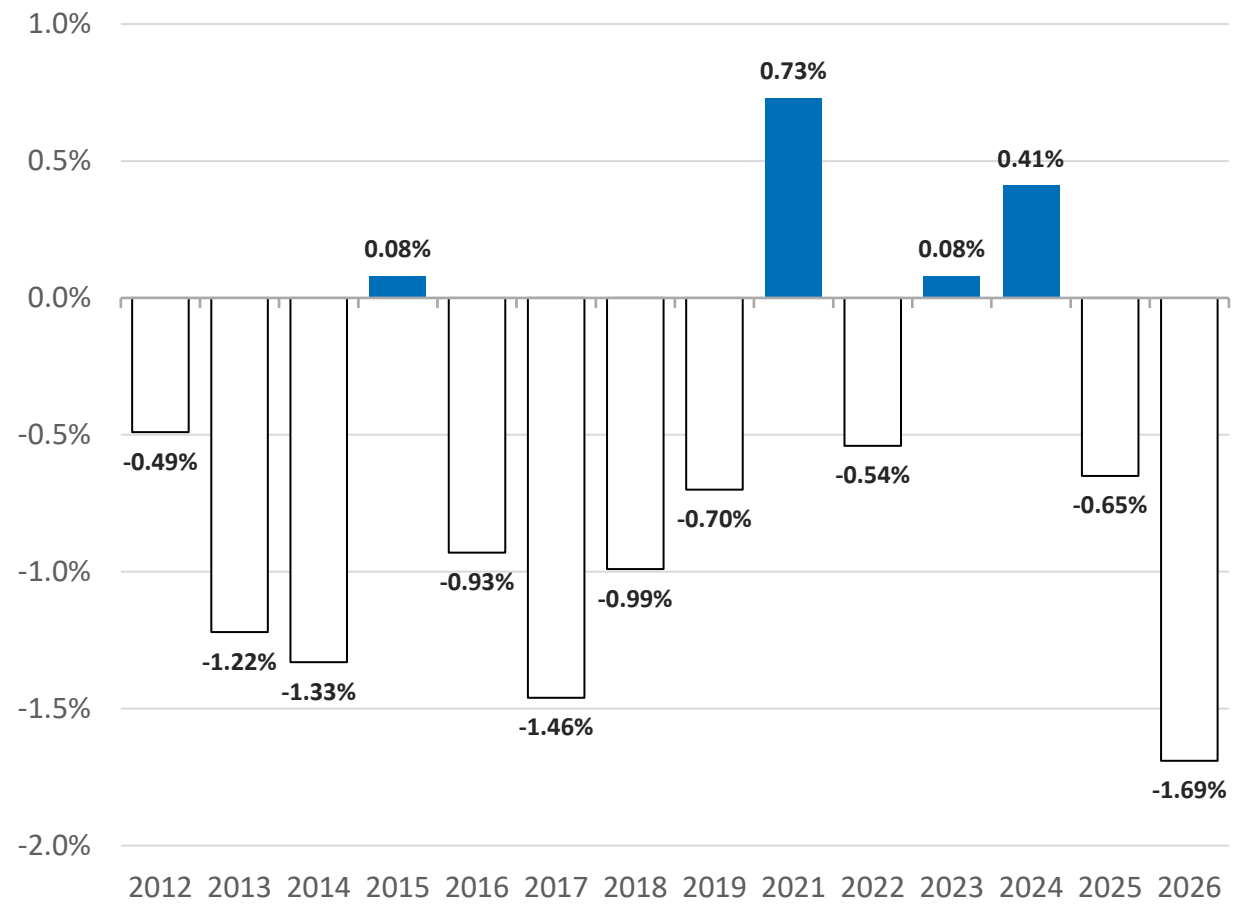
Second-quarter deposit runoff was the worst in years

Second-quarter % change in total deposits, by year (2020 excluded)



Source: Call report data via S&P Global; averages for U.S. banks under $10B.

–1.69%

average deposit change, 2Q26 (banks under $10B)

+$8B

increase in borrowings in 2Q26 to fill the gap

Key points

- Deposits usually dip in 2Q, but 2026's –1.69% was the largest 2Q decline since at least 2012
- It was also the steepest runoff of any quarter since 2023
- Loans were nearly flat, so loan-to-deposit ratios rose and borrowings climbed about $8B
- That sort of steady leak has to be funded somewhere

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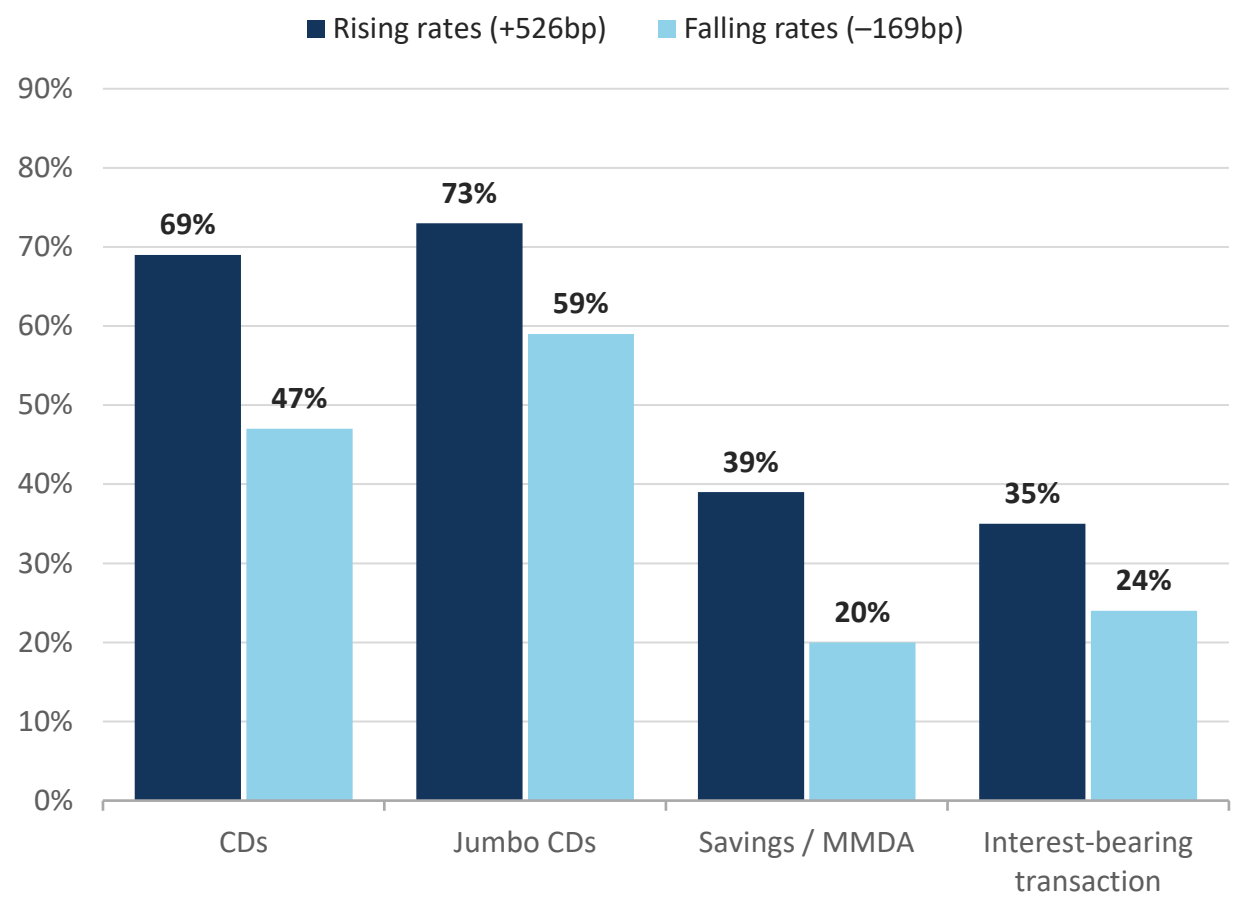
Deposits reprice up fast and down slowly

Deposit betas: share of the Fed's move passed through



1%

175bp of cuts over 21 months and IRRM data shows NMD cost is virtually unchanged — 0.68% to 0.67%.

41%

of IRRM institutions pay more on NMDs than at the 2024 peak

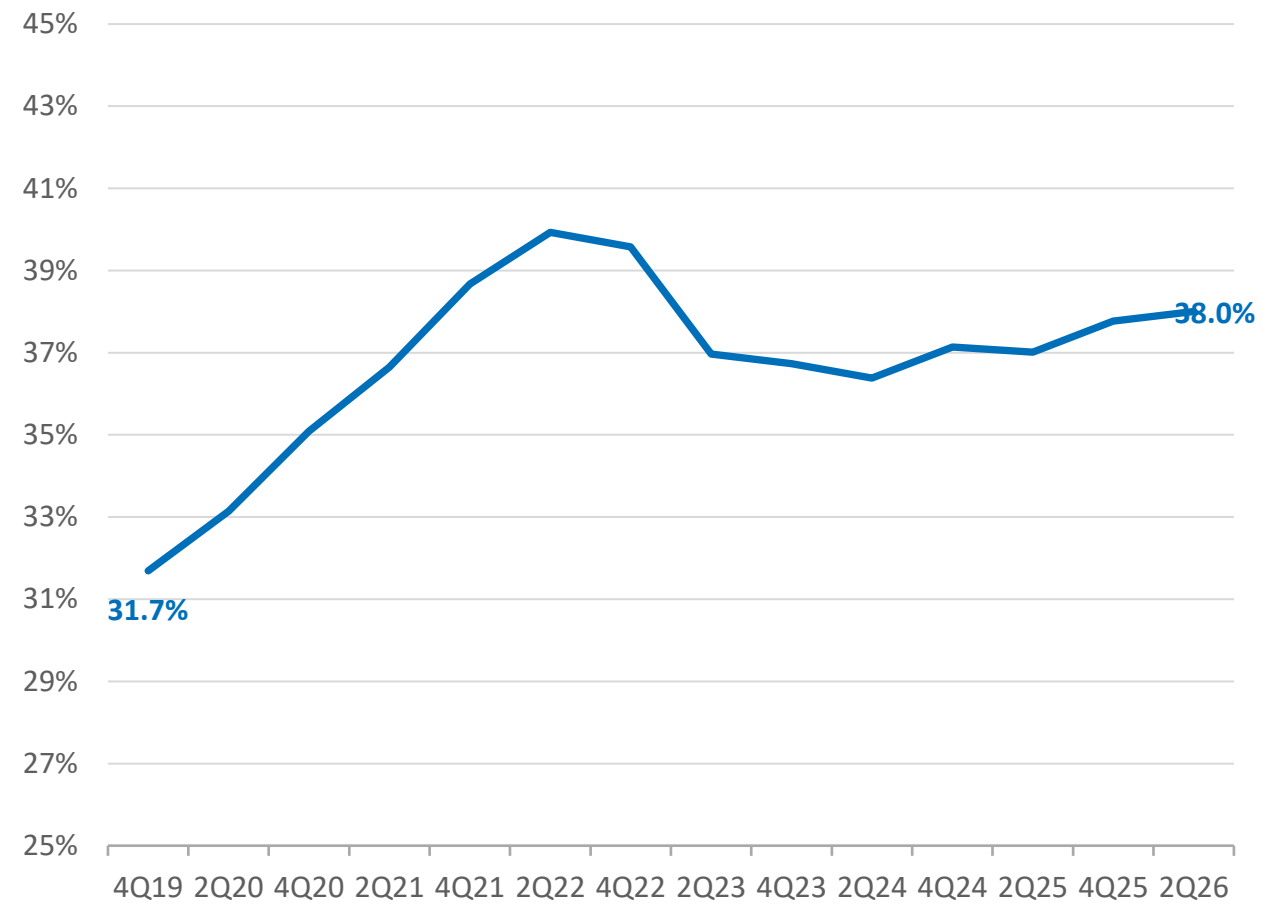
Key points

- Deposits followed the Fed up quickly but never followed it down
- With the Fed hiking again, potential pricing pressure would start from a higher base
- If deposit pricing lags the market, some rate-sensitive balances may move, a liquidity consideration as well as a margin one

Sources: Call report data via S&P Global and effective fed funds via FRED, St. Louis Fed (averages, banks under $10B); NMD figures: IRRM Reports (633 banks, through 8/26).

More deposits sit above the insurance limit

Deposits in accounts over $250K, share of domestic deposits (median)



Source: Call report data via S&P Global; median of U.S. banks under $10B in total assets (4,079 banks at 6/30/26).

Key points

- Balances over $250K rose from 32% of deposits in 2019 to 40% in 2022 but have only come down
- A close proxy for uninsured deposits, though not identical
- They move fastest in a stress, as in March 2023, but are often your best relationships
- Know who they are, how concentrated they are, and have a tool to insure them if needed (reciprocal deposits)

Know your big balances

- Top 20 depositors as a share of deposits
- Public funds and their collateral needs
- Balances over $250K by relationship

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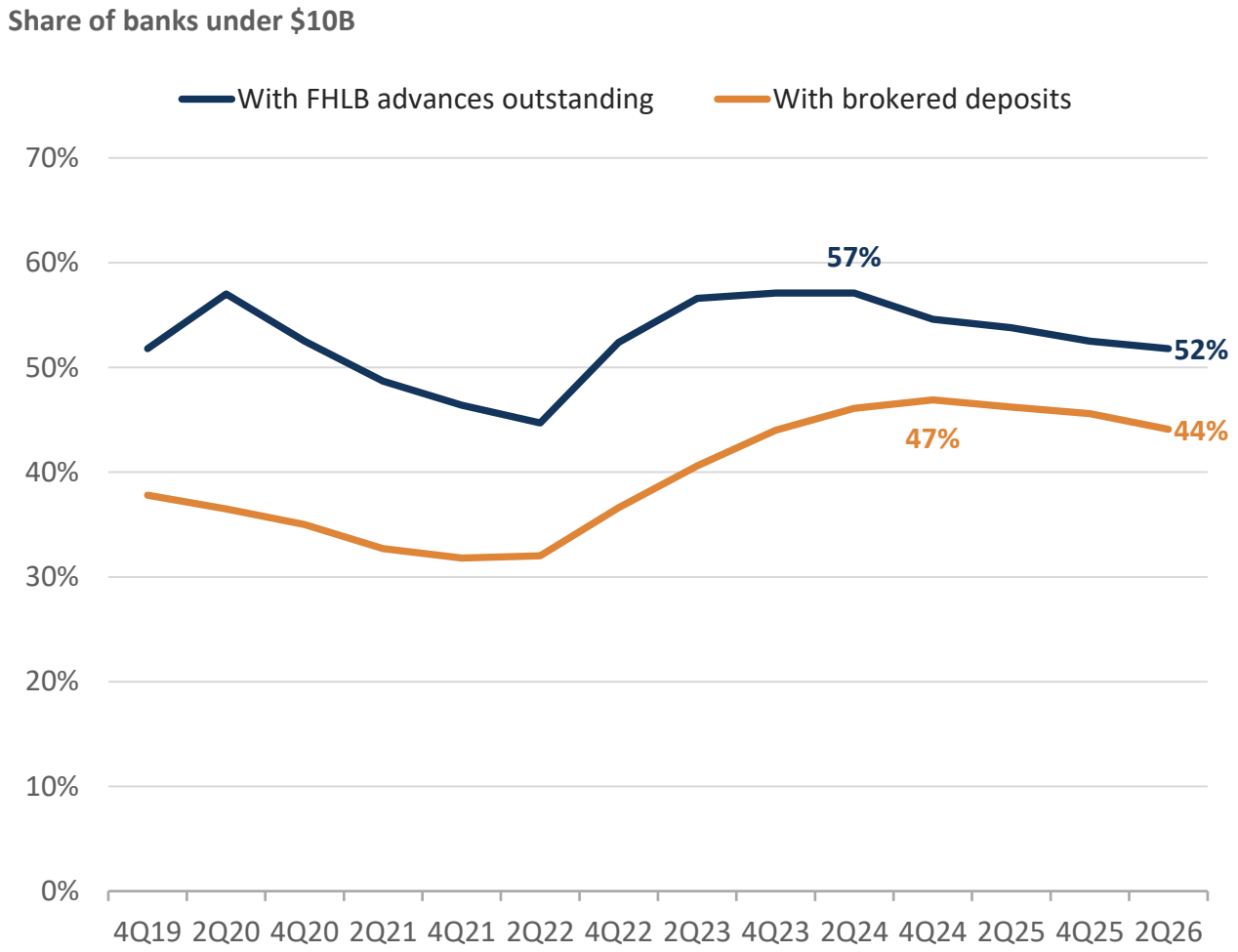
Wholesale funding has receded, but keep the lines warm



93%

of U.S. banks are FHLB members (U.S. GAO, 6/25)

2.8%

borrowed funds / assets, IRRM peers (2Q26)

Key points

- FHLB use peaked near 57% of banks in 2023–24 and is now 52%; about 44% use brokered deposits
- Borrowings are low (2.8% of assets for IRRM peers) but rose about $8B in 2Q26 as deposits ran off
- Unused lines go stale: collateral, agreements and staff know-how
- In 2020 and 2023 the FHLB worked for small banks that were already set up

Sources: Call report data via S&P Global (median, banks under $10B, 6/30/26); U.S. GAO, Federal Home Loan Banks: Role During Financial Stress (GAO-26-107373, 2026); IRRM Reports.

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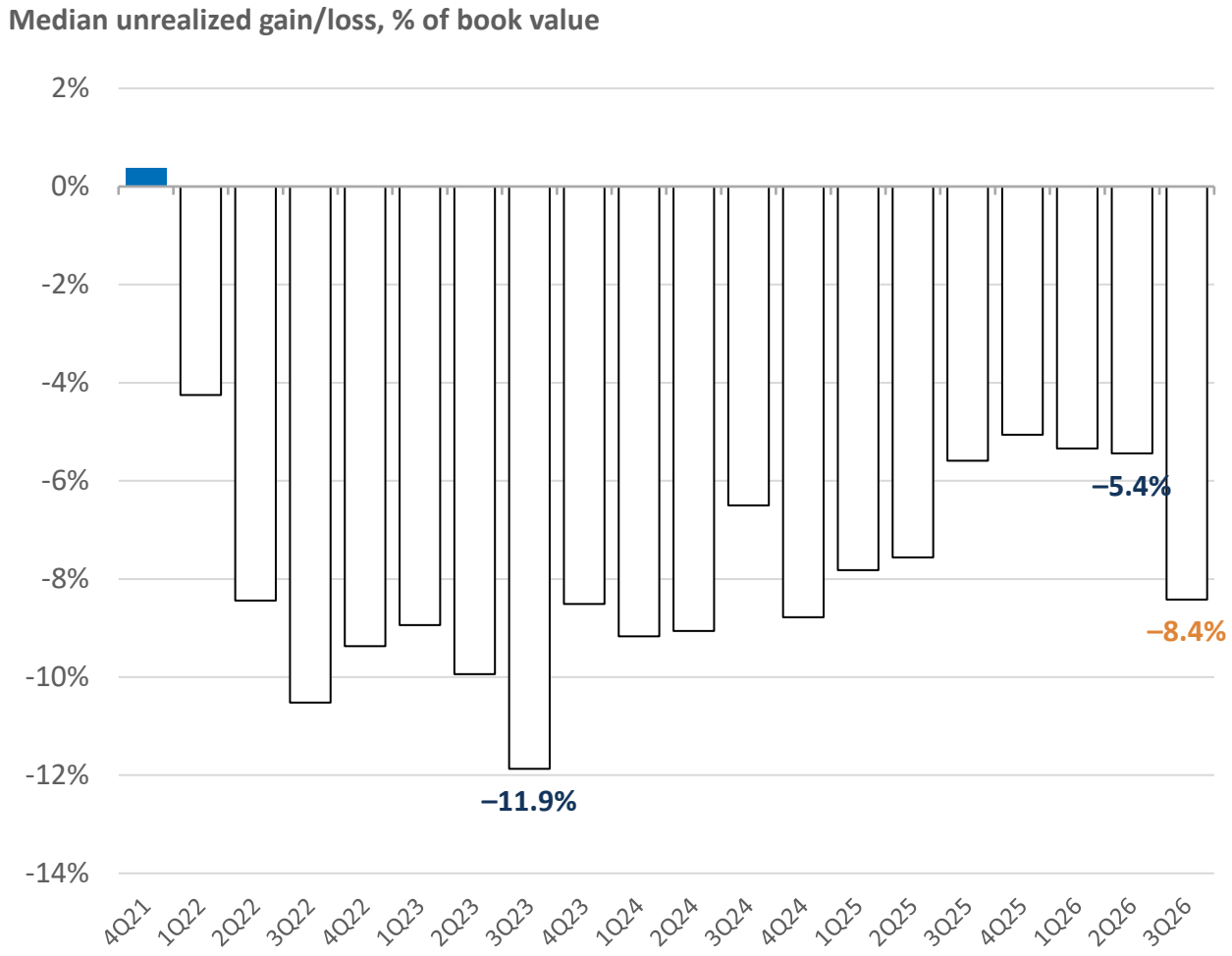
Your bond portfolio's liquidity has shifted



–8.4%

Median unrealized loss, 9/30/26

12.8%

of the portfolio returns as principal in the next 12 months

Key points

- Losses improved to about 5% by mid-2026, but the Q3 rate move pushed them back to 8.4%; 37% of portfolios are down more than 10%
- Selling bonds to raise cash locks in the loss, runs through earnings and reduces capital
- For liquidity, also focus on the principal your bonds pay back on their own (median BBA portfolio will return about 13% of its BV over the next 12 months)
- AND the ability to pledge those bonds as collateral to borrow from the FHLB or the discount window.

Source: BBA data; bank portfolios. 9/30/26 is preliminary (788 portfolios processed to date). Cash flow is base-case scheduled and projected principal.

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Contingency funding plans

Stress testing, early warnings and examiner expectations

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What examiners expect to see

1 Board-approved policy

Clear limits and risk tolerances, reviewed at least annually

2 Cash-flow stress testing

Forward-looking sources vs. uses across several scenarios and time horizons

3 Early-warning indicators

Named metrics, triggers and an owner who escalates

4 Tested funding sources

Lines drawn on, collateral pledged and documentation current

5 Discount window readiness

Agreements signed, collateral pledged, small test draw done

6 Board & ALCO reporting

Results the board understands, with action plans when limits are hit

The 2023 addendum's message: test your lines, be ready at the discount window, and count only what you can draw in a stress.

Sources: 2010 Interagency Policy Statement on Funding and Liquidity Risk Management; 2023 Addendum: Importance of Contingency Funding Plans (7/28/23); FDIC RMS Manual §6.1.

Adequately Capitalized: Contingent Funding Sources Are Affected

Funding Sources	FHLB Line (Secured)	Correspondent Bank Line (Unsecured)	FRB Discount Window Availability (Secured)	Listing Service Deposits	Brokered Deposits
Adequately Capitalized Effects	Collateral requirements change (haircuts and delivery)	Terminated due to deteriorated financial position	Reduced Line and/or higher collateral requirements	Restrictions per Part 337.6 (National Rate Caps)	Restrictions per Part 337.6 (Need waiver from FDIC to accept or renew)

Build stress tests around your own risks

1

PCA / credit stress

Capital falls below well capitalized: brokered and rate restrictions apply, FHLB capacity is cut, unsecured lines may be pulled

2

Local rate war

A competitor or online bank pays up; rate-sensitive and large balances leave

3

Rapid loan growth

Loan demand outruns deposits; on-balance-sheet liquidity is spent first

4

Rising rates, slower cash flow

Paydowns and prepayments slow just as loan demand and deposit costs rise

Ready-made rate-war test: The 3Q26 IRRM stress test moves 20% of NMDs into 6-month CDs; run it through your liquidity plan.

Sample Bank

3/31/2023

SHOCK: 0| 0 (12 Mo.)

Base Case

Dynamic Liquidity Monitor (DLM)

		Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	12Mo Totals
	Starting Cash Balances (Cash & Due & FFS)	36,576	33,334	30,093	26,727	23,562	20,858	17,539	14,371	11,134	8,080	4,930	1,800	
% Adj	**SOURCES**													
	Loan Maturities	8,657	4,432	7,248	2,871	2,493	7,310	12,109	2,922	10,442	2,223	8,562	10,465	79,734
	Loan Paydowns	6,323	6,416	6,124	6,223	6,145	5,878	6,000	5,683	5,804	5,699	5,269	5,516	71,080
	Investment Maturities & Prepayments	170	448	349	562	2,162	555	57	110	753	881	1,536	2,946	10,529
0%	New Deposits @ 0.00% Ann. Rate	-	-	-	-	-	-	-	-	-	-	-	-	-
85%	Time Deposit Renewals (85.00%)	10,496	14,408	20,088	11,728	8,222	20,359	4,708	9,400	8,120	15,394	23,514	11,807	158,244
90%	Migration from Time Deposits to NMD (90.00%)	1,667	2,288	3,190	1,863	1,306	3,234	748	1,493	1,290	2,445	3,735	1,875	25,133
	Renewal of Maturing FHLB Advances		15,000		30,000			20,000	20,000					85,000
	Total Projected Sources of Funds	**27,313**	**42,992**	**37,000**	**53,247**	**20,328**	**37,336**	**43,622**	**39,608**	**26,409**	**26,642**	**42,615**	**32,609**	**429,719**
% Adj	**USES**													
100%	Loan Cash Flow (100.00%)	14,980	10,848	13,372	9,094	8,638	13,188	18,109	8,605	16,246	7,922	13,831	15,981	150,814
3%	New Loans @ 3.00% Ann. Growth	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	24,049
	Net Change in Loans	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	24,049
75%	Investment Purchases (75.00%)	128	336	262	422	1,622	416	43	83	565	661	1,152	2,210	7,897
0%	New Securities @ 0.00% Ann. Growth	-	-	-	-	-	-	-	-	-	-	-	-	-
2%	NMD Runoff @ 2.00% Ann. Rate	1,095	1,095	1,095	1,095	1,095	1,095	1,095	1,095	1,095	1,095	1,095	1,095	13,137
	Time Deposit Maturities	12,348	16,950	23,633	13,798	9,673	23,952	5,539	11,059	9,553	18,111	27,663	13,890	186,169
	Borrowing Maturities	-	15,000		30,000			20,000	20,000					85,000
														-
	Total Projected Uses of Funds	**30,554**	**46,233**	**40,366**	**56,412**	**23,031**	**40,655**	**46,790**	**42,845**	**29,463**	**29,793**	**45,745**	**35,179**	**467,066**
	Projected Net Monthly Cash Flow	**(3,242)**	**(3,241)**	**(3,366)**	**(3,165)**	**(2,703)**	**(3,319)**	**(3,168)**	**(3,237)**	**(3,054)**	**(3,150)**	**(3,130)**	**(2,571)**	
	Cash Balance (Cash Liquidity)	**33,334**	**30,093**	**26,727**	**23,562**	**20,858**	**17,539**	**14,371**	**11,134**	**8,080**	**4,930**	**1,800**	**(770)**	
	Cash Balance / Total Assets	**2.9%**	**2.6%**	**2.3%**	**2.0%**	**1.8%**	**1.5%**	**1.2%**	**1.0%**	**0.7%**	**0.4%**	**0.2%**	**-0.1%**	
	Target - Cash Balance / Total Assets	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	
	Above Target?	**Yes**	**Yes**	**Yes**	**Yes**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	
	Primary Liquidity (Primary Liquidity = Cash Liquidity + Unpledged Inv. Port.)	**195,889**	**192,648**	**189,282**	**186,117**	**183,413**	**180,094**	**176,926**	**173,689**	**170,635**	**167,485**	**164,355**	**161,785**	
	Primary Liquidity / Total Assets	**16.8%**	**16.5%**	**16.3%**	**16.0%**	**15.8%**	**15.5%**	**15.2%**	**14.9%**	**14.7%**	**14.4%**	**14.1%**	**13.9%**	
	Target - Primary Liquidity / Total Assets	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	
	Above Target?	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	
	Total Liquidity (Primary + Secondary)	**645,889**	**642,648**	**639,282**	**636,117**	**633,413**	**630,094**	**626,926**	**623,689**	**620,635**	**617,485**	**614,355**	**611,785**	
	Total Liquidity / Total Assets	**55.5%**	**55.2%**	**54.9%**	**54.6%**	**54.4%**	**54.1%**	**53.8%**	**53.6%**	**53.3%**	**53.0%**	**52.8%**	**52.5%**	
	Target - Total Liquidity / Total Assets	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	
	Above Target?	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	

Available Funding Strategies (Secondary = Contingent Liquidity Sources)	Base Case	Stress
FHLB Availability (Secured)	250,000	-
Fed Discount Window (Secured)	50,000	-
Back-up Lines (Unsecured)	50,000	-
Brokered Deposits	100,000	-
Total Borrowing/Funding Availability	450,000	-

Starting Liquid Assets Breakdown	
Cash & Due	36,574
Fed Funds Sold	-
Securities	262,555
Less: Pledged Inv.	100,000
Total Liquid Assets	199,129

Sample Bank

3/31/2023

15% NMD Runoff Over 12 Months Stress Test

SHOCK: 0| 0 (12 Mo.)

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Dynamic Liquidity Monitor (DLM)

		Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	12Mo Totals
	Starting Cash Balances (Cash & Due & FFS)	36,576	26,219	15,862	5,380	(4,901)	(14,721)	(25,156)	(35,439)	(45,792)	(55,962)	(66,228)	(76,474)	
% Adj	**SOURCES**													
	Loan Maturities	8,657	4,432	7,248	2,871	2,493	7,310	12,109	2,922	10,442	2,223	8,562	10,465	79,734
	Loan Paydowns	6,323	6,416	6,124	6,223	6,145	5,878	6,000	5,683	5,804	5,699	5,269	5,516	71,080
	Investment Maturities & Prepayments	170	448	349	562	2,162	555	57	110	753	881	1,536	2,946	10,529
0%	New Deposits @ 0.00% Ann. Rate	-	-	-	-	-	-	-	-	-	-	-	-	-
85%	Time Deposit Renewals (85.00%)	10,496	14,408	20,088	11,728	8,222	20,359	4,708	9,400	8,120	15,394	23,514	11,807	158,244
90%	Migration from Time Deposits to NMD (90.00%)	1,667	2,288	3,190	1,863	1,306	3,234	748	1,493	1,290	2,445	3,735	1,875	25,133
	Renewal of Maturing FHLB Advances		15,000		30,000			20,000	20,000					85,000
	Total Projected Sources of Funds	**27,313**	**42,992**	**37,000**	**53,247**	**20,328**	**37,336**	**43,622**	**39,608**	**26,409**	**26,642**	**42,615**	**32,609**	**429,719**
% Adj	**USES**													
100%	Loan Cash Flow (100.00%)	14,980	10,848	13,372	9,094	8,638	13,188	18,109	8,605	16,246	7,922	13,831	15,981	150,814
3%	New Loans @ 3.00% Ann. Growth	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	24,049
	Net Change in Loans	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	24,049
75%	Investment Purchases (75.00%)	128	336	262	422	1,622	416	43	83	565	661	1,152	2,210	7,897
0%	New Securities @ 0.00% Ann. Growth	-	-	-	-	-	-	-	-	-	-	-	-	-
15%	NMD Runoff @ 15.00% Ann. Rate	8,211	8,211	8,211	8,211	8,211	8,211	8,211	8,211	8,211	8,211	8,211	8,211	98,526
	Time Deposit Maturities	12,348	16,950	23,633	13,798	9,673	23,952	5,539	11,059	9,553	18,111	27,663	13,890	186,169
	Borrowing Maturities	-	15,000		30,000			20,000	20,000					85,000
														-
	Total Projected Uses of Funds	**37,670**	**53,349**	**47,481**	**63,528**	**30,147**	**47,771**	**53,905**	**49,961**	**36,578**	**36,908**	**52,861**	**42,295**	**552,456**
	Projected Net Monthly Cash Flow	**(10,357)**	**(10,357)**	**(10,482)**	**(10,281)**	**(9,819)**	**(10,435)**	**(10,283)**	**(10,353)**	**(10,170)**	**(10,266)**	**(10,246)**	**(9,686)**	
	Cash Balance (Cash Liquidity)	**26,219**	**15,862**	**5,380**	**(4,901)**	**(14,721)**	**(25,156)**	**(35,439)**	**(45,792)**	**(55,962)**	**(66,228)**	**(76,474)**	**(86,160)**	
	Cash Balance / Total Assets	**2.3%**	**1.4%**	**0.5%**	**-0.4%**	**-1.3%**	**-2.2%**	**-3.0%**	**-3.9%**	**-4.8%**	**-5.7%**	**-6.6%**	**-7.4%**	
	Target - Cash Balance / Total Assets	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	**2.0%**	
	Above Target?	**Yes**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	**No**	
	Primary Liquidity (Primary Liquidity = Cash Liquidity + Unpledged Inv. Port.)	**188,774**	**178,417**	**167,935**	**157,654**	**147,834**	**137,399**	**127,116**	**116,763**	**106,593**	**96,327**	**86,081**	**76,395**	
	Primary Liquidity / Total Assets	**16.2%**	**15.3%**	**14.4%**	**13.5%**	**12.7%**	**11.8%**	**10.9%**	**10.0%**	**9.2%**	**8.3%**	**7.4%**	**6.6%**	
	Target - Primary Liquidity / Total Assets	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	**10.0%**	
	Above Target?	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**No**	**No**	**No**	**No**	
	Total Liquidity (Primary + Secondary)	**638,774**	**628,417**	**617,935**	**607,654**	**597,834**	**587,399**	**577,116**	**566,763**	**556,593**	**546,327**	**536,081**	**526,395**	
	Total Liquidity / Total Assets	**54.9%**	**54.0%**	**53.1%**	**52.2%**	**51.3%**	**50.4%**	**49.6%**	**48.7%**	**47.8%**	**46.9%**	**46.0%**	**45.2%**	
	Target - Total Liquidity / Total Assets	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	**20.0%**	
	Above Target?	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	

Available Funding Strategies (Secondary = Contingent Liquidity Sources)	Base Case	Stress
FHLB Availability (Secured)	250,000	-
Fed Discount Window (Secured)	50,000	-
Back-up Lines (Unsecured)	50,000	-
Brokered Deposits	100,000	-
Total Borrowing/Funding Availability	450,000	-

Starting Liquid Assets Breakdown	
Cash & Due	36,574
Fed Funds Sold	-
Securities	262,555
Less: Pledged Inv.	100,000
Total Liquid Assets	199,129

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Sample Bank

3/31/2023

SHOCK: 0| 0 (12 Mo.)

Less Than Well Capitalized Stress Test

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Dynamic Liquidity Monitor (DLM)

		Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	12Mo Totals
	Starting Cash Balances (Cash & Due & FFS)	36,576	28,955	21,335	13,590	6,046	(1,036)	(8,735)	(16,281)	(23,897)	(31,330)	(38,860)	(46,368)	
% Adj	SOURCES													
	Loan Maturities	8,657	4,432	7,248	2,871	2,493	7,310	12,109	2,922	10,442	2,223	8,562	10,465	79,734
	Loan Paydowns	6,323	6,416	6,124	6,223	6,145	5,878	6,000	5,683	5,804	5,699	5,269	5,516	71,080
	Investment Maturities & Prepayments	170	448	349	562	2,162	555	57	110	753	881	1,536	2,946	10,529
0%	New Deposits @ 0.00% Ann. Rate	-	-	-	-	-	-	-	-	-	-	-	-	-
85%	Time Deposit Renewals (85.00%)	10,496	14,408	20,088	11,728	8,222	20,359	4,708	9,400	8,120	15,394	23,514	11,807	158,244
90%	Migration from Time Deposits to NMD (90.00%)	1,667	2,288	3,190	1,863	1,306	3,234	748	1,493	1,290	2,445	3,735	1,875	25,133
	Renewal of Maturing FHLB Advances		15,000		30,000			20,000	20,000					85,000
	Total Projected Sources of Funds	27,313	42,992	37,000	53,247	20,328	37,336	43,622	39,608	26,409	26,642	42,615	32,609	429,719
% Adj	USES													
100%	Loan Cash Flow (100.00%)	14,980	10,848	13,372	9,094	8,638	13,188	18,109	8,605	16,246	7,922	13,831	15,981	150,814
3%	New Loans @ 3.00% Ann. Growth	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	24,049
	Net Change in Loans	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	2,004	24,049
75%	Investment Purchases (75.00%)	128	336	262	422	1,622	416	43	83	565	661	1,152	2,210	7,897
0%	New Securities @ 0.00% Ann. Growth	-	-	-	-	-	-	-	-	-	-	-	-	-
10%	NMD Runoff @ 10.00% Ann. Rate	5,474	5,474	5,474	5,474	5,474	5,474	5,474	5,474	5,474	5,474	5,474	5,474	65,684
	Time Deposit Maturities	12,348	16,950	23,633	13,798	9,673	23,952	5,539	11,059	9,553	18,111	27,663	13,890	186,169
	Borrowing Maturities	-	15,000		30,000			20,000	20,000					85,000
														-
	Total Projected Uses of Funds	34,933	50,612	44,745	60,791	27,410	45,034	51,169	47,224	33,842	34,172	50,124	39,558	519,613
	Projected Net Monthly Cash Flow	(7,621)	(7,620)	(7,745)	(7,544)	(7,082)	(7,698)	(7,547)	(7,616)	(7,433)	(7,529)	(7,509)	(6,950)	
	Cash Balance (Cash Liquidity)	28,955	21,335	13,590	6,046	(1,036)	(8,735)	(16,281)	(23,897)	(31,330)	(38,860)	(46,368)	(53,318)	
	Cash Balance / Total Assets	2.5%	1.8%	1.2%	0.5%	-0.1%	-0.8%	-1.4%	-2.1%	-2.7%	-3.3%	-4.0%	-4.6%	
	Target - Cash Balance / Total Assets	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	
	Above Target?	Yes	No	No	No	No	No	No	No	No	No	No	No	
	Primary Liquidity (Primary Liquidity = Cash Liquidity + Unpledged Inv. Port.)	191,510	183,890	176,145	168,601	161,519	153,820	146,274	138,658	131,225	123,695	116,187	109,237	
	Primary Liquidity / Total Assets	16.4%	15.8%	15.1%	14.5%	13.9%	13.2%	12.6%	11.9%	11.3%	10.6%	10.0%	9.4%	
	Target - Primary Liquidity / Total Assets	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	
	Above Target?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	No	
	Total Liquidity (Primary + Secondary)	461,510	453,890	446,145	438,601	431,519	423,820	416,274	408,658	401,225	393,695	386,187	379,237	
	Total Liquidity / Total Assets	39.6%	39.0%	38.3%	37.7%	37.1%	36.4%	35.8%	35.1%	34.5%	33.8%	33.2%	32.6%	
	Target - Total Liquidity / Total Assets	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	
	Above Target?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	

Available Funding Strategies (Secondary = Contingent Liquidity Sources)	Base Case	Stress
FHLB Availability (Secured)	250,000	225,000
Fed Discount Window (Secured)	50,000	45,000
Back-up Lines (Unsecured)	50,000	Terminated
Brokered Deposits	100,000	Restricted
Total Borrowing/Funding Availability	450,000	270,000

Starting Liquid Assets Breakdown	
Cash & Due	36,574
Fed Funds Sold	-
Securities	262,555
Less: Pledged Inv.	100,000
Total Liquid Assets	199,129

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Early-warning indicators: an example framework

Example levels only: not recommendations. Set your own triggers in policy based on your bank's risk profile.

Indicator	Green: monitor	Yellow: ALCO reviews	Red: activate CFP
Loans / deposits	*e.g., below 80%*	*e.g., 80–85%*	*e.g., above 85%*
Liquid assets / total assets	*e.g., above 15%*	*e.g., 10–15%*	*e.g., below 10%*
Wholesale funding reliance	*e.g., below 10%*	*e.g., 10–15%*	*e.g., above 15%*
Deposit outflow in a month	*e.g., under 2%*	*e.g., 2–5%*	*e.g., over 5%*
Securities pledged	*e.g., under 50%*	*e.g., 50–70%*	*e.g., over 70%*
Capital	*e.g., well capitalized with cushion*	*e.g., near internal minimum*	*e.g., below well capitalized*

The structure is the point: each indicator gets a level, an owner and a required action.

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Liquidity sources & tools

What's available, how fast, and what changed in 2026

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Know your liquidity stack, in the order you'd use it

		Speed	Reliability in a stress
1	**On balance sheet** Cash, fed funds sold, unpledged securities, portfolio cash flow	Same day	High
2	**Secured borrowing** FHLB advances, Fed discount window, repo	Same day to 2 days	High if collateral is pledged
3	**Deposit tools** Reciprocal, brokered, listing-service deposits	Days to weeks	Brokered restricted if capital slips
4	**Unsecured lines** Correspondent fed funds lines	Same day	Low: first to be cut

For each layer ask: How much is really available? How fast? Will it still be there if my bank is the one in trouble?

Reciprocal deposits: the cap just got much bigger

	Before	Now
Cap on reciprocals treated as non-brokered	Lesser of $5B or 20% of total liabilities	**Tiered: 50% of the first $1B of liabilities, 40% of the next $9B, 30% above (max $30B)**
CAMELS composite rating (must also be well capitalized)	1 or 2	**1, 2 or 3**
Community banks over the cap (KC Fed est., 6/30/26)	About 7%	**Fewer than 1%**

Key dates

July 11, 2026
21st Century ROAD to Housing Act takes effect

Sept. 1, 2026
FDIC interim final rule takes effect

Oct. 1, 2026
Comment period closed

Next
Final rule: watch for any changes

What to do: Not in a network? Consider getting set up. Already in one? Revisit your CFP and brokered deposit limits.

Sources: FDIC interim final rule, 91 FR 56022 (9/1/26); Federal Reserve Bank of Kansas City Community Banking Bulletin. Not legal advice; confirm treatment with your regulator.

FHLB and discount window: two lines, one collateral plan

FHLB

~90%

of banks rank FHLB advances first for secured funding

93%

of U.S. banks are FHLB members

- Know borrowing capacity after haircuts
- Confirm capacity under a PCA stress, when haircuts rise
- Test overnight and term draws annually

Discount window

88%

of surveyed banks are operationally ready

4.00%

primary credit rate after 9/16/26

- Sign agreements and pledge collateral before you need it
- Use the simpler borrower-in-custody process
- Make a small test draw at least annually

The SVB lesson: collateral at the FHLB couldn't move to the Fed fast enough. Plan where collateral goes, and test both.

Sources: ABA DataBank (March 2026); U.S. GAO report GAO-26-107373; FOMC implementation note (9/16/26); ABA Banking Journal on the Fed's BIC program update (8/10/26).

Best practices checklist for ALCO

1 Benchmark to banks your size

Not industry aggregates driven by the largest banks

2 Re-run stress tests for higher rates

Slower cash flows, costlier deposits, lower bond values

3 Count portfolio cash flow as a source

Know your 12-month principal and what's unpledged

4 Confirm borrowing capacity after haircuts

FHLB and discount window, including under a PCA stress

5 Test every line, every year

Small draws on the FHLB, discount window and fed funds lines

6 Revisit reciprocal deposits

New cap: 50% of the first $1B of liabilities

7 Put numbers and names on EWIs

Green / yellow / red triggers, each with an owner

8 Report it so the board can act

Limits, results and action plans in plain language

Today's IRR Management Trends and Best Practices

The Baker Group

Where Are Rates Going?



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IRRM NIC and EVE Peer Data

633 institutions processed on IRRM as of Q2 2026, a statistically meaningful cross-section of community banks

- Median institution now shows a negative change in net interest income (NIC) if rates fall — a notable reversal from recent history where most banks were positioned to benefit from falling rates.
- Median institution's EVE is now more negatively impacted in falling scenarios than in prior quarters as well.

Statistics based on 633 banks.

Earnings at Risk: 12-Month Net Interest Income, Parallel Shocks

Scenario	Largest loss	25th percentile	Median	75th percentile	Largest gain
-300	-16%	-4%	-2%	0%	9%
-200	-11%	-3%	-1%	0%	5%
-100	-6%	-2%	-1%	0%	3%
+100	-3%	0%	0%	1%	6%
+200	-7%	-1%	1%	2%	11%
+300	-9%	-2%	1%	3%	16%

Economic Value of Equity, Parallel Shocks

Scenario	Largest loss	25th percentile	Median	75th percentile	Largest gain
-300	-38%	-13%	-5%	3%	37%
-200	-22%	-6%	-1%	5%	30%
-100	-10%	-2%	1%	4%	18%
+100	-21%	-6%	-3%	-1%	7%
+200	-43%	-14%	-8%	-3%	11%
+300	-65%	-21%	-13%	-6%	14%

Data pulled from IRRM Reports, reflects real time positions and assumptions

The balance-sheet positioning that made sense the last several quarters is now creating a different risk profile.

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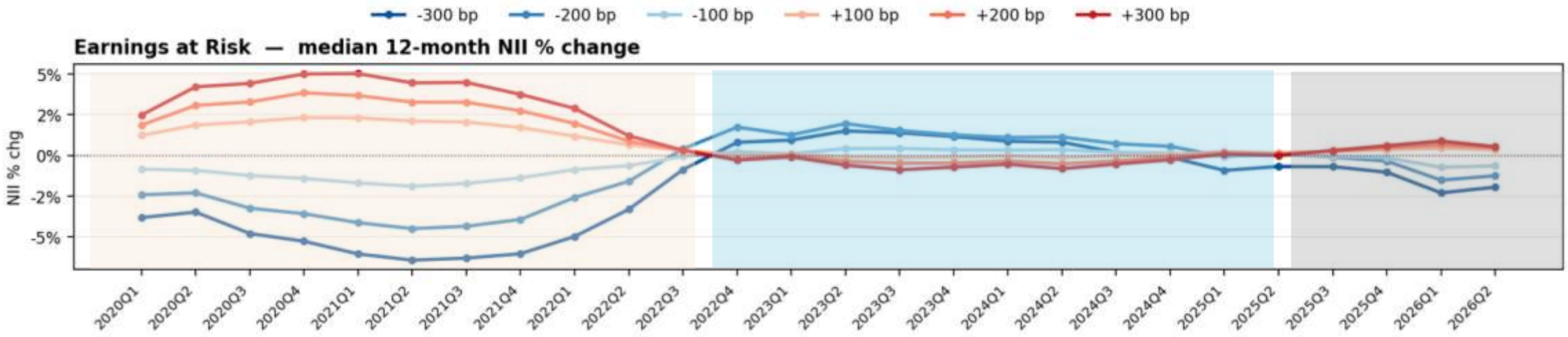
IRRM NIC and EVE Peer Data (2020-2026)

Median institution's NIC sensitivity from 2020 through Q2 2026



Source: IRRM Reports; values are % change vs. the unchanged base.

Pre-2022 asset-sensitive, low-rate era.

2022 flip to liability-sensitive as rates begin to increase rapidly, deposits got expensive, and lower yield fixed rated loans slow to reprice higher.

2025 reversal back toward asset-sensitivity as COVID-era loans reprice up and funding costs normalized.

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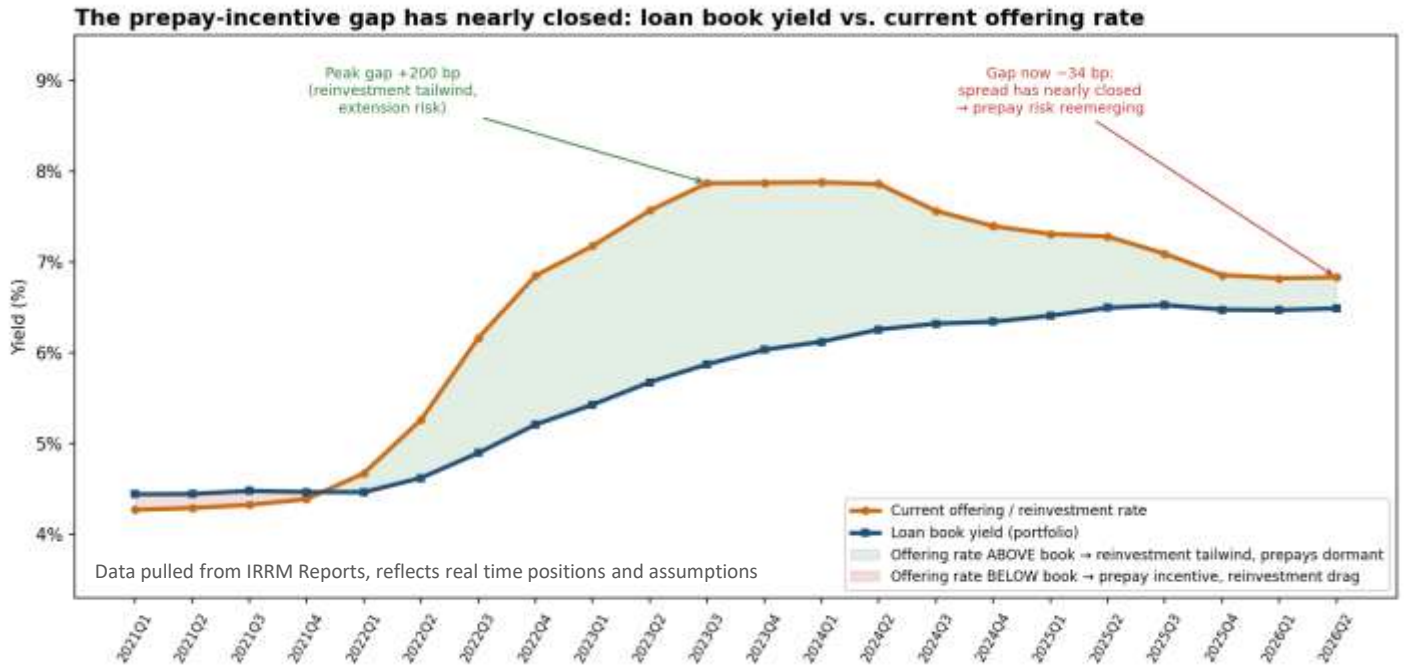
What Examiners Are Looking For – *Prepayment Speeds*

- Are the prepayment speed assumptions reasonable in light of the bank's product mix, business strategy, historical experience, and competitive market?
- Are prepayment speeds adjusted based on different rate scenarios (i.e. faster when rates fall, slower when rates rise vs. flat across rate scenarios)?
- Does the institution regularly back-test the assumptions against actual performance?
- If provided by a third-party, how does management determine that the prepayment speeds are appropriate for the bank's products?



Loan yields have nearly caught up to offering rates — the spread that suppressed prepays is mostly gone



Why it matters

— 2022–23: offering rates ran as much as **~200 bp above** book yields → maturing loans reinvested higher (NIM tailwind) and below-market loans stayed put (extension).

— Today the gap is **~34 bp** — the reinvestment tailwind is largely spent and prepay protection is thin.

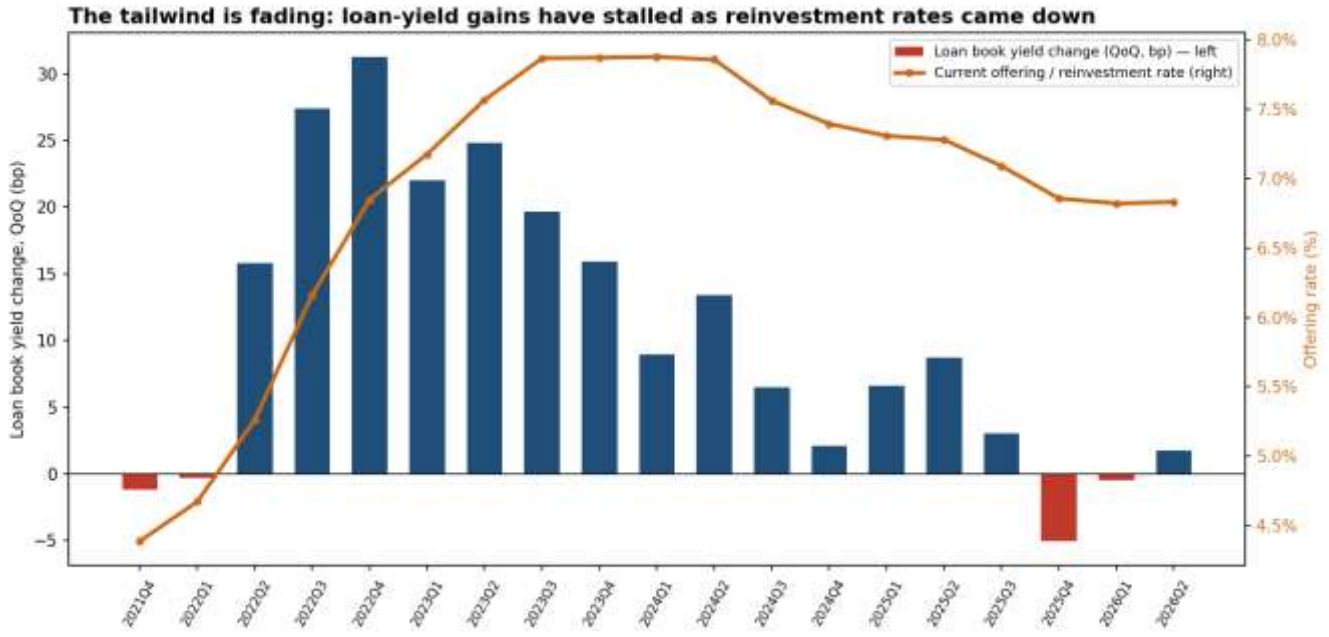
Both of those protections are mostly gone:

- The NIM tailwind from loan repricing is essentially exhausted
- Borrowers are no longer meaningfully out-of-the-money to refinance — any further rate drop tips the prepayment risk calculus.

The spread that masked prepayment risk for two years has mostly closed.

The repricing tailwind has stalled — loan yields are flat

THE TREND — Quarterly changes in average loan book yield from 2022 through Q2 2026.



Data pulled from IRRM Reports, reflects real time positions and assumptions

What you're seeing

— Loan book-yield gains peaked at **+31 bp/qtr (2022Q4)** and have faded to roughly zero.

— Q4 2025: loan yield actually **ticked down** (−5 bp) as offering rates fell; Q1 was flat and Q2 2026 added back just +2 bp.

— In Q4 / Q1, NIM held up because **funding repriced down faster** — and in Q2 2026 funding costs stopped falling.

- At the peak, a $200M loan book was adding roughly $625K/year in annual interest income purely from portfolio repricing.
- Over the last three quarters the average loan yield has gone flat: down 5 bp in Q4, flat in Q1, up 2 bp in Q2.
- NIM has kept expanding, but the driver has changed; in Q4 and Q1 it was held up almost entirely by funding costs repricing down.

Funding costs flattened in Q2 — if they bottom out or reaccelerate, there is no longer a loan repricing buffer to absorb it. Understand which driver is sustaining margin because the forward risk profile looks materially different than it did two years ago.

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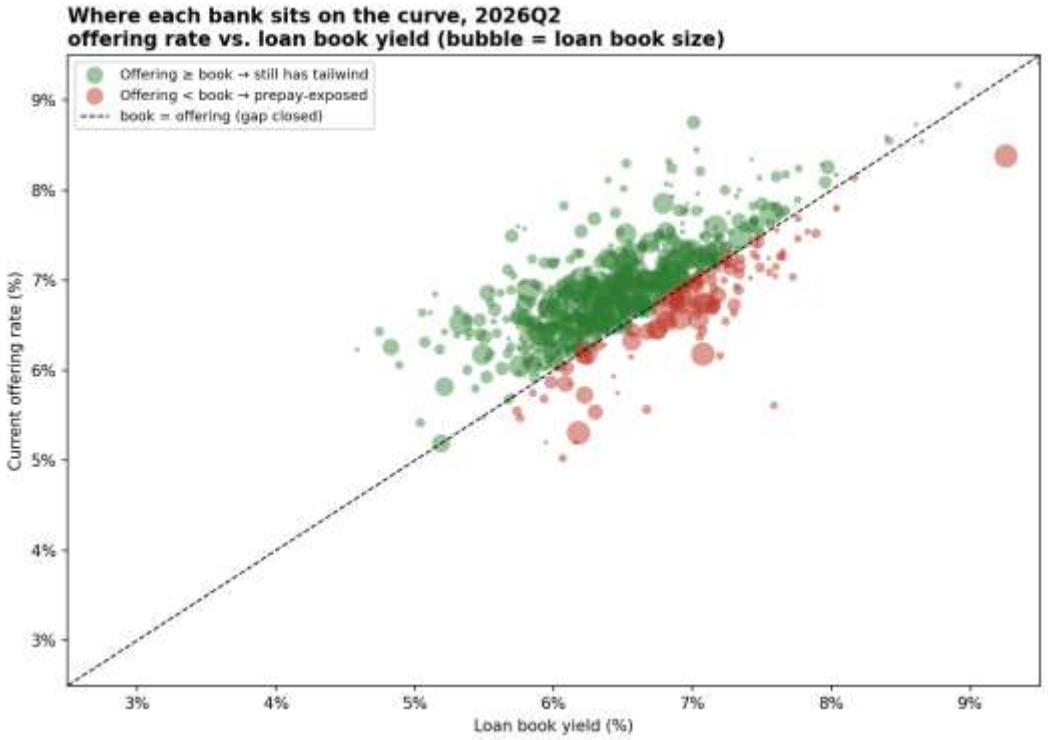
Two banks, same margin, very different places on the curve



Data pulled from IRRM Reports, reflects real time positions and assumptions

Where you sit

— Green (offering ≥ book): still has **repricing tailwind** — low-coupon books (2020–21 growers).

— Red (offering < book): booked **at/above market** (2023–24 growers) — prepay-exposed now.

— Know which side you're on ***before*** setting prepay assumptions.

- Green dots: current offering rate is ABOVE the current book yield (still repricing loans up, banks that grew books heavily in 2020–2021)
- Red dots: offering rate is BELOW book yield (booked heavily in 2023–2024 at or near rate peaks — more prepayment risk today).

This is why institution-specific assumptions matter — two banks with the same NIM can have fundamentally different prepayment risk profiles.

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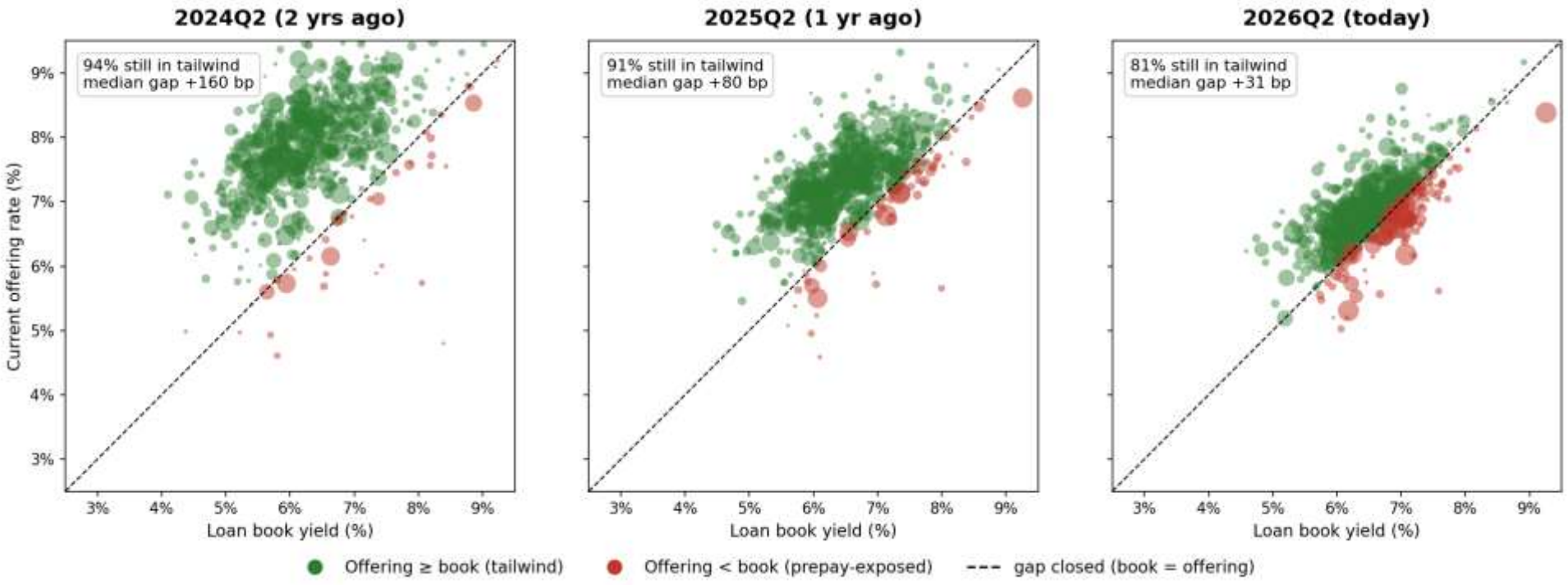
How we got here: the tailwind was nearly universal two years ago — it's compressing fast



Data pulled from IRRM Reports, reflects real time positions and assumptions

Median offer-over-book gap: **+160 bp → +80 bp → +31 bp** · Banks still in tailwind: **94% → 91% → 81%** — and the cloud is dispersing along the curve.

The trend is clear: the share of institutions with offering rates above book yields is down 13 points, and the median spread has shrunk by 129 bps in two years.

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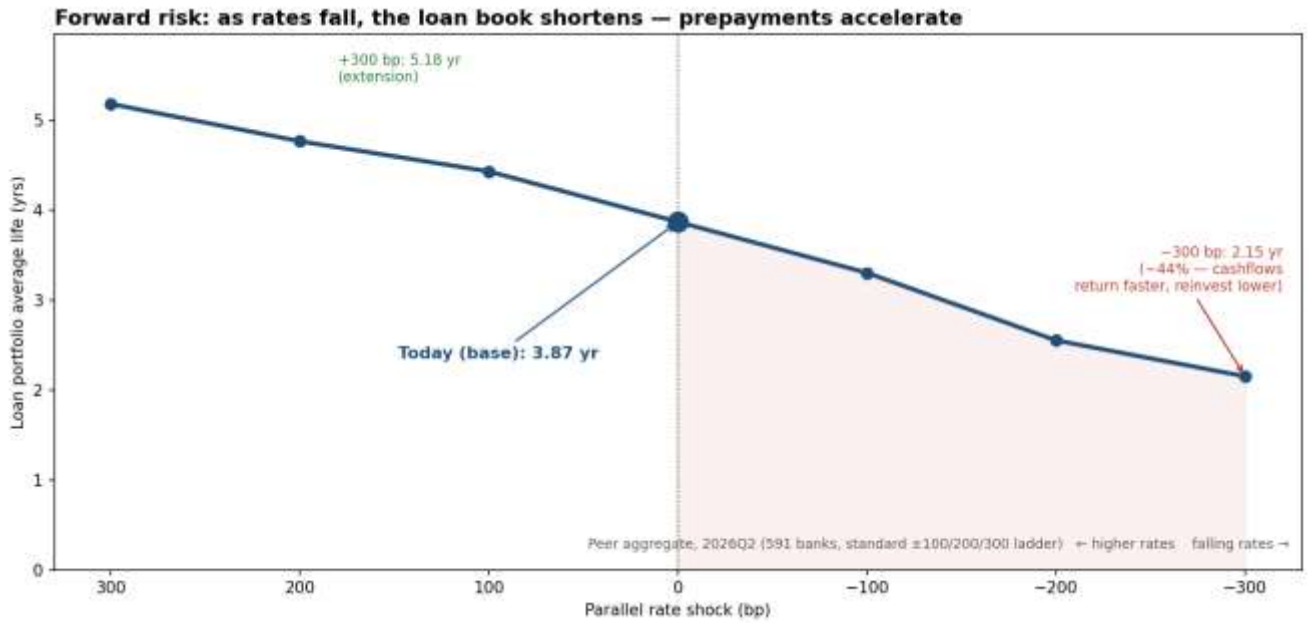
If rates fall, the loan book shortens fast — cashflows return early, reinvest lower



Data pulled from IRRM Reports, reflects real time positions and assumptions

The prepay mechanism

— Base average life ~3.9 yr; a **–300 bp shock cuts it to ~2.2 yr (–44%)**.

— Faster cashflows + lower reinvestment rate = a **direct hit to loan NIC**.

— The duration institutions tried to lock in **unwinds on its own** through prepayments.

- For institutions that are in the 'red' (offering rate below book yield), this risk is already present at current rates.
- Even a 50–100 bp cut could meaningfully accelerate prepayments.

This is why stress-testing higher CPR scenarios is so important — it directly informs how much rate risk the institution is carrying.

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Position early: revisit assumptions, stress prepays, understand risks

01

Revisit CPR assumptions

Many were set for the low-prepay regime of '23–24. That era is ending — stale CPRs overstate duration and understate prepay risk.

02

Stress higher prepay speeds

Model what happens if prepayments move meaningfully higher to see the true average-life and NIC exposure.

03

Position from strength

The shift is gradual and NIM is at a 7-year high. Recognizing it early is what keeps you ahead of it.

Interest-rate risk management is an ongoing process — what worked the last two years may not be what works the next two.

What Examiners Are Looking For – *Deposit Assumptions*



- **Has management analyzed the bank's customer base and reasonable assumptions given the bank's performance, marketing, and pricing strategies?**
- **Are the deposit assumptions based on internal historical data or industry benchmarks?**
  - If using a Beta Analysis to compare historical performance of core deposit rates compared to FF, has there been consideration or adjustment to account for differences between current environment and historical?
  - If using an Open Close Study to analyze the tenor of current and recently closed accounts, has there been a factor adjustment to reduce true historical average lives for conservatism and the rise of mobile banking?
  - If using industry benchmarks, have they been adjusted for institution-specific customer dynamics?
- **Do assumptions reflect known differences in rate sensitivity and customer behavior by product (e.g. NOW, MMDA, savings, interest-bearing DDA)?**
- **Are deposit assumptions stress tested (e.g., using higher betas, shorter lives) to evaluate model sensitivity?**
- **Are static or outdated assumptions being used (i.e. not adjusted to reflect the current rate environment)?**
- **Are all deposit assumptions formally documented—including data sources, rationale, segmentation, and update frequency?**



Deposits Are Not Following the Fed Down

Falling 2024–Current • Fed Funds 5.50% → 3.75%

	Peak	Trough	Change	Beta
Fed Funds	5.50%	3.75%	**-1.75%**	**100%**
Total NMD	0.68%	0.67%	-0.01%	**1%**
NOW	0.58%	0.72%	+0.14%	**-8%**
Money Market	1.65%	1.62%	-0.03%	**2%**
Savings	0.38%	0.35%	-0.03%	**1%**
Total CD	4.17%	3.47%	-0.70%	**40%**

What this says

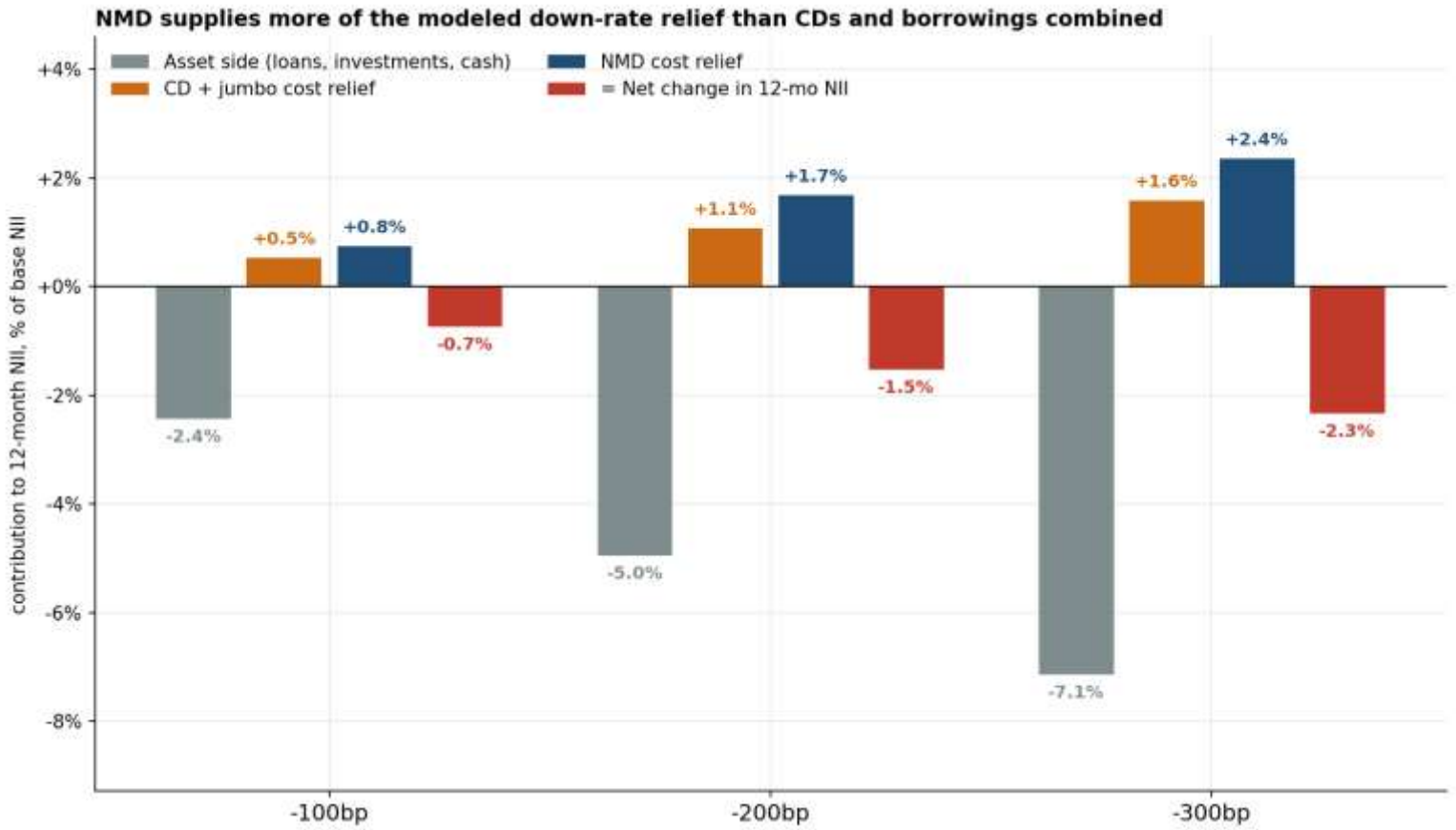
— 175bp of cuts over 21 months and the typical institutions's NMD cost is **unchanged** — 0.68% to 0.67%.

— NOW accounts are still **going up** (-8% beta). Money market sits at 1.62%, near its cycle high.

— The deposit relief that did arrive came from CDs.

— **41% of institutions pay more on their NMDs today than at the 2024 peak.**

NMD Carries Most of the Down-Rate Relief When Modeled



Straight out of the model

— At −300bp the asset side costs the median bank **-7.1% of NII**. NMD relief hands back +2.4% which is more than CDs and borrowings combined.

— NMD supplies **55% of all modeled funding relief** and offsets 32% of the asset-side drag.

— Take that relief away and the median −300bp NIC goes from **-2.3% → -5.1%**.

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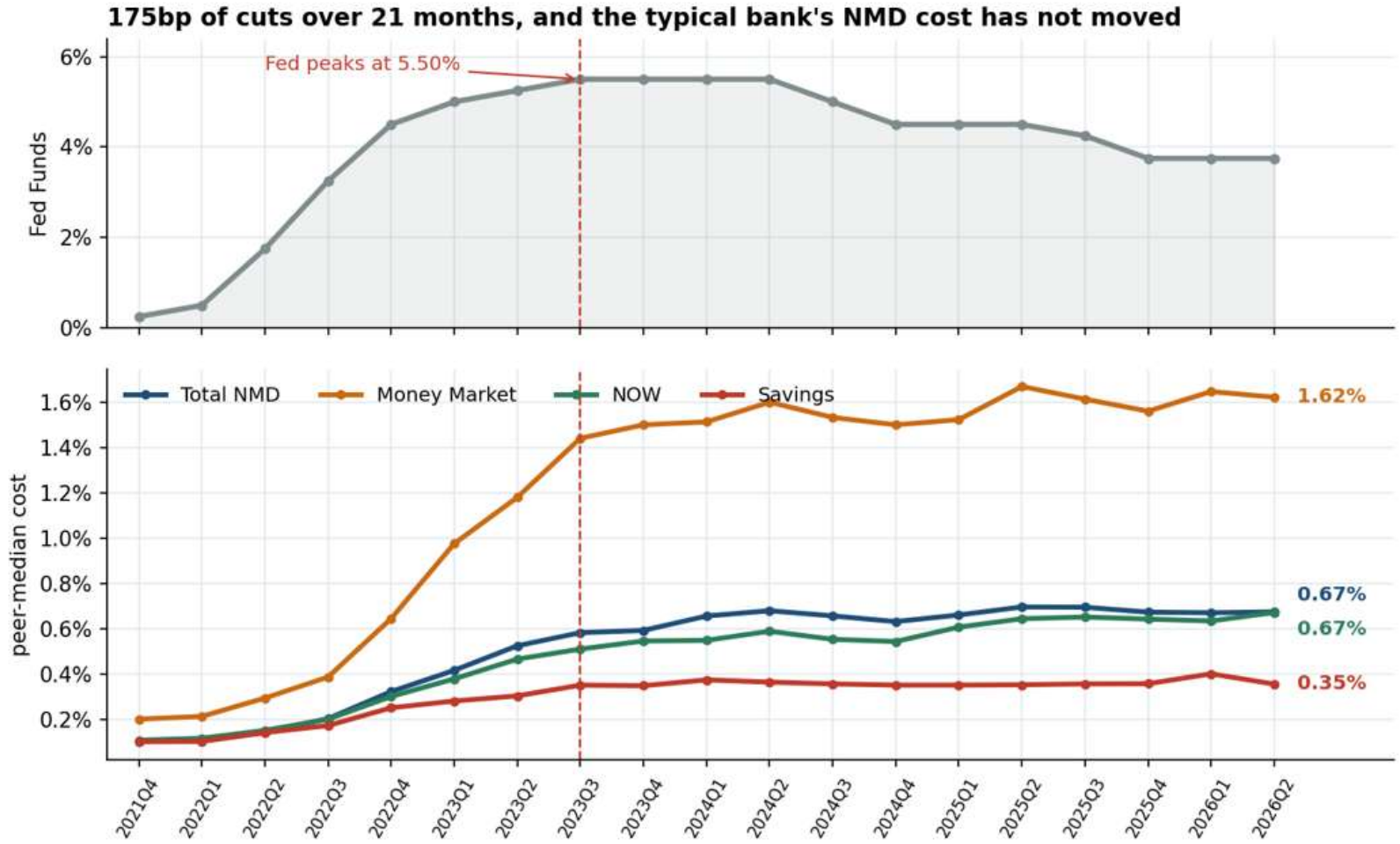
If Rates Rise, the Pressure Is Worse



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Non-Maturing Deposit Analysis: Deposit Overview

#1 Rising Rates: Q1 2004 to Q3 2006 - FF Increased 425bps												
	2004Q1	2004Q2	2004Q3	2004Q4	2005Q1	2005Q2	2005Q3	2005Q4	2006Q1	2006Q2	2006Q3	Beta
NOW	0.57	0.43	0.45	0.57	0.57	0.56	0.58	0.66	0.75	0.75	0.91	8%
SVG/MM	1.06	0.92	1.01	1.10	1.13	1.13	1.05	0.98	1.50	2.11	2.61	25%
Fed Funds	1.00	1.25	1.75	2.25	2.75	3.25	3.75	4.25	4.75	5.25	5.25	

#2 Falling Rates: Q2 2007 to Q1 2010 - FF Decreased 500bps													
	2007Q2	2007Q3	2007Q4	2008Q1	2008Q2	2008Q3	2008Q4	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	Beta
NOW	0.81	0.80	0.82	0.82	0.66	0.65	0.36	0.27	0.30	0.28	0.36	0.34	11%
SVG/MM	3.04	3.08	2.81	2.00	1.35	1.34	0.83	0.65	0.68	0.70	0.73	0.73	50%
Fed Funds	5.25	4.75	4.25	2.25	2.00	2.00	0.25	0.25	0.25	0.25	0.25	0.25	

#3 Rising Rates: Q3 2015 to Q4 2018 - FF Increased 225bps															
	2015Q3	2015Q4	2016Q1	2016Q2	2016Q3	2016Q4	2017Q1	2017Q2	2017Q3	2017Q4	2018Q1	2018Q2	2018Q3	2018Q4	Beta
NOW	0.13	0.12	0.12	0.12	0.13	0.15	0.14	0.15	0.16	0.18	0.17	0.22	0.23	0.25	6%
SVG/MM	0.14	0.13	0.14	0.13	0.16	0.15	0.15	0.20	0.19	0.20	0.22	0.29	0.29	0.33	9%
Fed Funds	0.25	0.50	0.50	0.50	0.50	0.75	1.00	1.25	1.25	1.50	1.75	2.00	2.25	2.50	

#4 Falling Rates: Q2 2019 to Q4 2021 - FF Decreased 225bps												
	2019Q2	2019Q3	2019Q4	2020Q1	2020Q2	2020Q3	2020Q4	2021Q1	2021Q2	2021Q3	2021Q4	Beta
NOW	0.24	0.30	0.32	0.26	0.16	0.16	0.17	0.16	0.16	0.16	0.16	6%
SVG/MM	0.34	0.37	0.41	0.38	0.26	0.25	0.26	0.25	0.23	0.23	0.22	6%
Fed Funds	2.50	2.00	1.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	

#5 Rising Rates: Q1 2022 to Q2 2024 - FF Increased 500bps											
	2022Q1	2022Q2	2022Q3	2022Q4	2023Q1	2023Q2	2023Q3	2023Q4	2024Q1	2024Q2	Beta
NOW	0.15	0.17	0.50	0.93	1.11	1.25	1.47	1.67	1.56	1.48	30%
SVG/MM	0.22	0.22	0.31	0.57	1.13	1.01	0.84	0.75	0.50	0.51	13%
Fed Funds	0.50	1.75	3.25	4.50	5.00	5.25	5.50	5.50	5.50	5.50	
NOW Qtr Beta		2%	22%	34%	36%	56%	88%				
SVG/MM Qtr Beta		0%	6%	21%	112%	-48%	-68%				

#6 Falling Rates: Q3 2024 to Current					
	2024Q3	2024Q4	2025Q1	2025Q2	Beta
NOW	1.52	1.50	1.25	1.38	29%
SVG/MM	0.51	0.49	0.46	0.52	4%
Fed Funds	5.00	4.50	4.50	4.50	

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Beta Analysis

Analysis compares historical performance of core deposit rates compared to Fed Funds

From a historical perspective, core deposit rates have typically lagged the market by a range of 15-30%

Currently, falling rate betas are particularly important to model IRR effectively

Table 1d: All Banks – Non-Maturity Deposit Assumptions

Deposit type	–100 BPs repricing rates 25th percentile	–100 BPs repricing rates median	–100 BPs repricing rates 75th percentile	+100 BPs repricing rates 25th percentile	+100 BPs repricing rates median	+100 BPs repricing rates 75th percentile	Average lives 25th percentile	Average lives median	Average lives 75th percentile
Money market deposit account	24%	35%	50%	25%	35%	52%	2.50	3.83	5.00
NOW/ interest checking	10%	18%	31%	12%	19%	30%	3.55	4.94	7.03
Savings	10%	15%	26%	10%	15%	25%	4.00	5.00	6.98
Non-interest bearing	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable	3.97	5.00	6.58

Falling Rates 2007 to 2010	Peak	Trough	Change	Beta
Fed Funds	5.25	0.25	-5.00	100%
NOW	1.22	0.46	-0.76	15%
SAVINGS	2.00	0.49	-1.51	30%
MMDA	4.19	0.85	-3.34	67%

Rising Rates 2015 to 2018	Trough	Peak	Change	Beta
Fed Funds	0.25	2.50	2.25	100%
NOW	0.02	0.30	0.28	12%
SAVINGS	0.10	0.56	0.46	20%
MMDA	0.11	0.85	0.74	33%

Falling Rates 2019 to 2020	Peak	Trough	Change	Beta
Fed Funds	2.50	0.25	-2.25	100%
NOW	0.45	0.06	-0.39	17%
SAVINGS	0.54	0.06	-0.48	21%
MMDA	1.04	0.14	-0.90	40%

Rising Rates 2022 to 2024	Trough	Peak	Change	Beta
Fed Funds	0.25	5.50	5.25	100%
NOW	0.03	0.48	0.45	9%
SAVINGS	0.04	1.31	1.27	24%
MMDA	0.05	3.14	3.09	59%

Falling Rates 2024 to Current	Peak	Trough	Change	Beta
Fed Funds	5.00	4.25	-0.75	100%
NOW	0.39	0.37	-0.02	3%
SAVINGS	1.25	1.10	-0.15	20%
MMDA	3.13	2.96	-0.17	23%

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Open Close Study

Open close study analyzes current and recently closed accounts

Critical assumption for EVE analysis, especially for institutions with higher weights of NMDs

Historically, community-based institutions have exhibited average lives greater than what is used in most ALM models

A conservative approach is to use a factor adjustment to reduce the true historical average lives

Acct ID	Type Code	Open Date	Closed Date (If App)	Balance	Avg Life	Factor Adj Avg Life
1	MMKT	01/12/1958	12/09/2025	$24,795.48	67.95	33.98
2	MMKT	09/20/1963	12/09/2025	$2,523.20	62.26	31.13
3	MMKT	01/15/1968	12/09/2025	$870.00	57.94	28.97
4	MMKT	11/24/1980	12/09/2025	$3,891.10	45.07	22.54
5	MMKT	12/30/1980	12/09/2025	$393.19	44.97	22.49
6	MMKT	10/21/1981	12/09/2025	$5,430.44	44.16	22.08
7	MMKT	03/29/1982	12/09/2025	$267.68	43.73	21.86
8	MMKT	06/25/1982	12/09/2025	$44,501.26	43.49	21.74
9	MMKT	12/02/1982	12/09/2025	$3,232.19	43.05	21.52
10	MMKT	01/06/1983	12/09/2025	$81,455.06	42.95	21.48
11	MMKT	01/06/1983	12/09/2025	$56,753.19	42.95	21.48
12	MMKT	01/17/1983	12/09/2025	$10,010.08	42.92	21.46
13	MMKT	01/25/1983	12/09/2025	$6,093.63	42.90	21.45
14	MMKT	02/14/1983	12/09/2025	$1,350.40	42.85	21.42

List Product Name	0 - 3 M	3 - 12 M	1 - 3 Yr	3 - 5 Yr	5 - 10 Yr	10 + Yr	Avg Life	Total %	Total Bal
MMKT	1%	26%	13%	6%	13%	41%	7.75	100%	$40,616,797
Savings	0%	4%	13%	11%	9%	62%	10.75	100%	$42,274,412
NOW	0%	1%	7%	7%	7%	78%	12.65	100%	$55,923,374
DDA	0%	2%	17%	8%	12%	61%	10.73	100%	$27,281,043

Factor Adjustment 50%

List Product Name	0 - 3 M	3 - 12 M	1 - 3 Yr	3 - 5 Yr	5 - 10 Yr	10 + Yr	Avg Life	Total %	# Accts
MMKT	6%	29%	14%	10%	21%	20%	5.45	100%	4249
Savings	2%	13%	16%	7%	19%	43%	8.59	100%	1935
NOW	0%	3%	13%	6%	19%	59%	10.76	100%	1117
DDA	0%	10%	18%	11%	28%	33%	7.89	100%	782

What Next?

01

Back-test your assumptions

— Back test your expected Change in Interest Expense over the last 12 months versus actual results.

— If the back tests expected a beta of 15-35% and you realized 1%, look at why. Is it time to adjust your assumptions?

02

Break the symmetry

— It is easy to model one beta in both directions. In IRR modeling, we want to see different betas in rising and falling scenarios.

— Understand your betas in different rate scenarios as well. You may be more rate sensitive in a +300 environment versus a +100 environment.

03

Don’t assume Cost of Funds relief is coming

— Stress test your NMD betas and understand the impact to earnings and EVE.

— It may feel unrealistic, but it is better to be safe than sorry.

IRRM Benchmark and Assumptions Peer Data

Where does my policy limit stand relative to peers?

Policy Risk Limits for Parallel Shocks

	12-month, net interest income (policy limit)			Economic value of equity (policy limit)		
	25th percentile	Median	75th percentile	25th percentile	Median	75th percentile
–300	–20%	–20%	–20%	–40%	–35%	–30%
–200	–15%	–15%	–15%	–30%	–30%	–20%
–100	–12%	–12%	–10%	–20%	–20%	–10%
+100	–12%	–12%	–10%	–20%	–20%	–10%
+200	–15%	–15%	–15%	–30%	–25%	–20%
+300	–20%	–20%	–20%	–40%	–35%	–30%

Non-Maturity Deposit Assumptions

	–100 BPs repricing rates			+100 BPs repricing rates			Average lives		
	25th	Median	75th	25th	Median	75th	25th	Median	75th
Money market deposit account	35%	35%	35%	35%	35%	37%	2.81	2.83	4.21
NOW/interest checking	15%	15%	25%	15%	15%	27%	2.87	3.50	5.80
Savings	15%	15%	15%	15%	15%	15%	5.72	6.36	6.95
Non-interest bearing	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable	4.75	5.18	6.15

Every institution is different but if your assumptions or limits look like outliers relative to the benchmarks, that is a useful starting point for an assumption review conversation with your IRR provider.

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IRRM Model Reporting

Each Quarter – "Regulatory Report"

- Q2 2026 update: a new 'Steepener' scenario has been added to the Regulatory Report
- Bear Steepener where short-end rates rise +50 bp and long-end rates rise +100 bp
- Market is increasingly pricing in a scenario where long-end Treasury yields (driven by supply/demand and inflation expectations) rise faster than the Fed-controlled short end.

Parallel	Bull Steepener	Bull Steepener	*Unchanged*	Steepener	Bear Flattener	Parallel
-400/ -400 bp (1)	-200/ -100 bp (2)	-100/ 0 bp (3)	*Rate*	+50/+100 bp (5)	+200/+100 bp (6)	+400/+400 bp (7)
0 Mo.	12 Mo.	12 Mo.	*Scenario*	12 Mo.	12 Mo.	0 Mo.

Each Quarter – "Immediate Rate Shock Reports"

- Useful for capital adequacy and EVE analysis.
- Parallel ramps test gradual rate moves over 12 months — more realistic for earnings simulations.

Immediate	Immediate	Immediate	*Unchanged*	Immediate	Immediate	Immediate
-300/ -300 bp (1)	-200/ -200 bp (2)	-100/ -100 bp (3)	*Rate*	+100/+100 bp (5)	+200/+200 bp (6)	+300/+300 bp (7)
0 Mo.	0 Mo.	0 Mo.	*Scenario*	0 Mo.	0 Mo.	0 Mo.

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IRRM Model Processing Schedule – 2026

1st Quarter – CD Beta Stress

- 20% Betas in Falling Rate Scenarios
- All time lags at 0 months

2nd Quarter 2026 – NMD Beta Stress Test

- Increase all rising rate scenario betas up to 75% (if current beta is < 75%) & adjust all NMD Time lags to 0 month (if current lag > 1 month)
- Decrease all falling rate scenario betas to 0%

3rd Quarter – NMD Migration Stress

- 20% of NMDs migrated to 6 Mo CDs

4th Quarter – Liability Avg Stress Test

- Back Test December 2025 to December 2026
- Reduce NMD average lives by 50%

Importance of Stress Testing In Today's Environment

Stress Testing helps plan against unlikely events

- Example: Deposit Betas over the last rising rate cycle

Stress Testing helps identify vulnerabilities early

- Helps the bank understand how its balance sheet—especially earnings and capital—perform under rate environments, allowing the bank to proactively manage potential risks rather than react to problems after they occur.

Stress Testing helps the institution make informed decisions

- Even modest rate shocks can have outsized impacts so stress testing can inform decisions about balance sheet composition, deposit pricing, funding diversification, etc.

Stress Testing allows the institution to refine model assumptions

- Highlights how sensitive projected outcomes are to core assumptions so the institution can focus attention on validating or refining those assumptions.

Examiners like to see a proactive Stress Testing process

- Regulators expect community banks to use stress testing—not just to "check a box," but as a meaningful tool to:
  - Evaluate capital adequacy
  - Test the sensitivity of earnings and value to rate movements
  - Ensure policies reflect actual risk capacity and tolerance

Identifying Appropriate Stress Tests

- **Look back at past rate cycles/economic environments (Ex: 2008 GFC, Covid, Dot Com Bubble)**
- **Analyze differences/similarities in the Balance sheet**
  - Has deposit composition shifted? How has Cost of Funds changed?
- **Think about what may happen over a 12-month horizon**
  - Rate cuts? Hikes? Sticky NMD/CD Yields? Increase in loan paydowns?
- **Isolate a few key assumptions/scenarios**
- **Model and stress these scenarios utilizing your ALM model**
  - Remember, these do not have to be overly complicated stresses. Pick one assumption and analyze the impact.

Recommendations – Interest Rate Risk Management

- **Assumption Development**
  - Institution Specific Assumptions
  - Support & Documentation of Assumptions
  - Core Deposit Study (Beta and Open/Close)
- **Backtesting**
  - Understand your most recent backtest and any significant variances.
- **Assumption Reviews**
  - Use backtest to jump start those reviews.
  - Document these reviews. How will the assumptions be adjusted or not adjusted?
  - More frequent assumption review in current falling rate environment.
- **Stress / Sensitivity Test Key Assumptions**
  - Decrease falling scenario beta factors on NMDs and CDs
  - Reduce average lives on NMDs
  - Migrate a % of NMD into wholesale funding (stressed simulation)
  - Change loan prepayment speeds
- **Annual Independent Review of ALCO Process**

Introduction to Derivatives

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Every balance sheet carries interest rate risk

When rates move, what a bank earns on its assets and what it pays for its funding don't always move together. That mismatch is interest rate risk.

When rates rise

Deposit and borrowing costs climb quickly, while fixed-rate loans and bonds keep earning the same rate.

Margins get squeezed at liability-sensitive banks

When rates fall

Floating-rate loans and new investments earn less, while some deposit costs can't fall much further.

Margins get squeezed at asset-sensitive banks

Traditional tools change what you lend, invest in, or borrow. **Derivatives** are one more tool: a way to adjust rate risk without changing the underlying loans, securities or deposits.

What is an interest rate derivative?



A contract between two parties whose value is based on ("derived from") an interest rate.

Think of it like a fixed-price agreement or an insurance policy for interest rates.

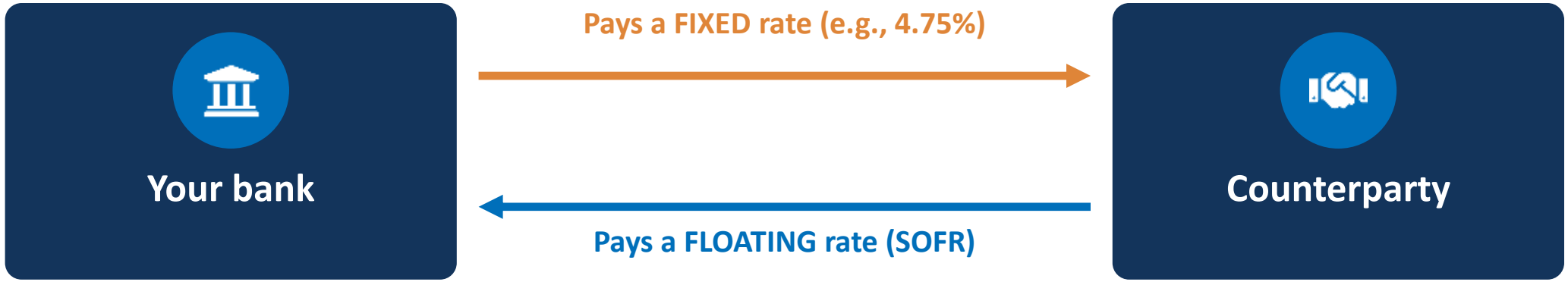
No loan principal changes hands. The parties only exchange interest payments.

Five terms to know

1. **Notional amount:** The reference amount used to calculate payments. It is never exchanged.
2. **Fixed rate:** A rate set on day one that stays the same for the life of the contract.
3. **Floating rate:** A rate that resets with the market. SOFR is the most common benchmark today.
4. **Counterparty:** The other side of the contract, typically a large bank or swap dealer.
5. **Hedge:** A position taken to offset a risk you already have.

A swap trades one type of interest payment for another

An interest rate swap is an agreement to exchange interest payments on the same notional amount for a set period of time.



Same notional, no principal

Both payments are calculated on the same reference amount, which never changes hands.

Only the difference is paid

Payments are netted. Whoever owes more pays the difference each period.

Works in either direction

A bank can pay fixed and receive floating, or receive fixed and pay floating.

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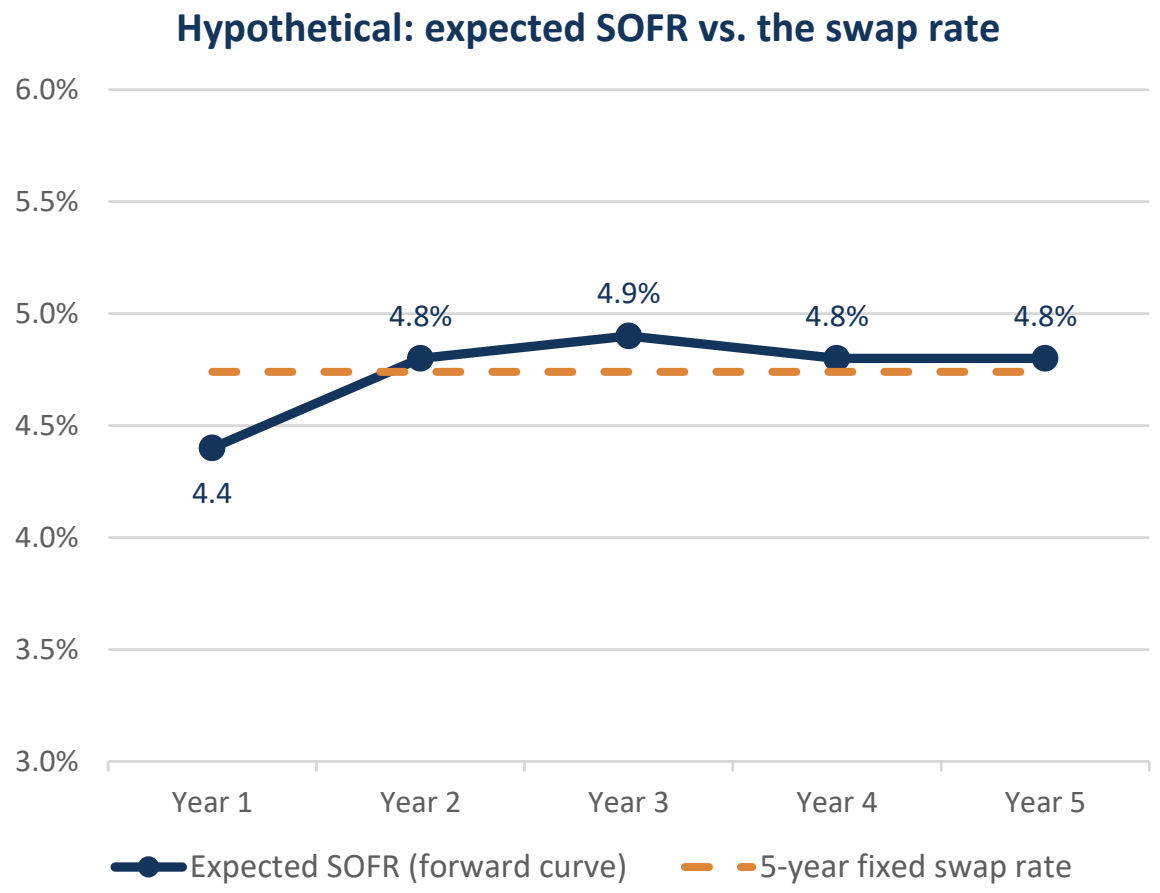
Where does the fixed swap rate come from?

1. The market has an expectation for where SOFR will be in each future period. This is called the forward curve.

2. The fixed swap rate is roughly the average of those expected rates over the life of the swap.

3. So on day one, neither side is expected to come out ahead. A new swap starts with a value of about zero.



Swap rate ≈ average of expected SOFR ≈ 4.74%. Expectations change daily, so swap rates do too.

Hypothetical rates, for illustration only.

Example: turning a floating funding cost into a fixed one

The situation

A bank funds $10 million of loans with short-term borrowings that reprice with SOFR.

The swap

It agrees to pay 4.75% fixed and receive SOFR on a $10 million notional.

4.75%

net funding cost, wherever SOFR goes

SOFR	Borrowing cost	Swap: received / (paid)	Net annual cost
3.75%	$375,000	($100,000)	**$475,000**
4.25%	$425,000	($50,000)	**$475,000**
5.25%	$525,000	$50,000	**$475,000**
6.25%	$625,000	$150,000	**$475,000**

As SOFR rises, the borrowing gets more expensive, but the swap pays the bank more.

As SOFR falls, the borrowing gets cheaper, but the bank pays more on the swap.

Hypothetical, for illustration only. Assumes the borrowing rate equals SOFR; excludes spreads, fees and collateral.

A swap's value changes as rates move

Example: a bank agrees to pay 4.75% fixed on a 5-year swap. A year later, market swap rates have changed.

Market rates rise to 5.75%

The bank is locked in at a below-market 4.75%. Someone would pay to take over that swap.

The swap has positive value (an asset)

Market rates fall to 3.75%

The bank is locked in at an above-market 4.75%. It would have to pay to get out of the swap.

The swap has negative value (a liability)

Why it matters: a change in value isn't paid in cash unless the swap is ended early, but it can require posting collateral and may affect capital or earnings, depending on the accounting. The value drifts back toward zero as the swap nears maturity.

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Caps, floors and collars work like insurance

Cap

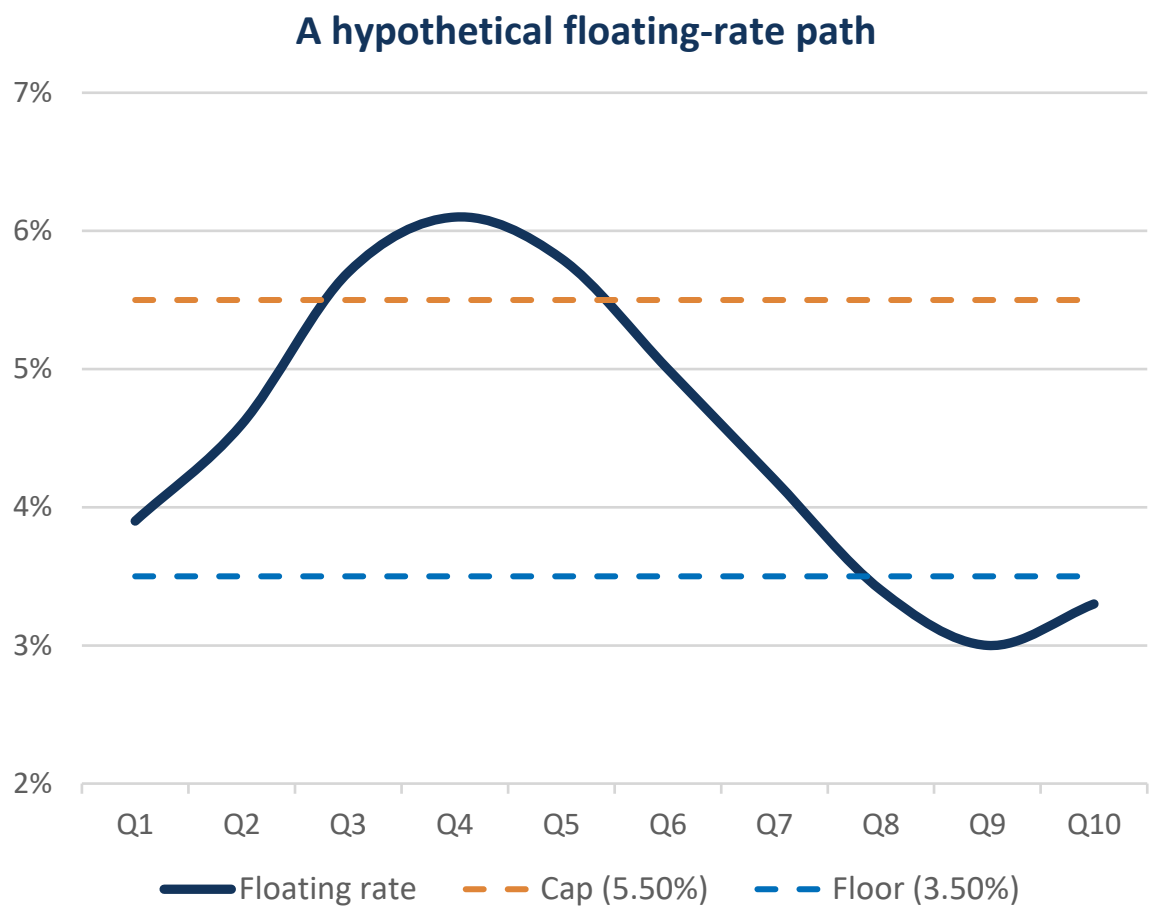
Sets a ceiling on a floating rate. If rates rise above it, the cap pays the difference. Costs an upfront premium.

Floor

Sets a minimum on a floating rate. If rates fall below it, the floor pays the difference. Also costs an upfront premium.

Collar

Buy one and sell the other. Your effective rate stays within a band, and the option sold offsets some or all of the cost.



Above the cap or below the floor, the option pays. In between, nothing happens.

Hypothetical rate path, for illustration only.

Example: putting a ceiling on funding costs

The situation

The same bank funds $10 million with short-term borrowings that reprice with SOFR.

The cap

It pays an upfront premium for a 5.50% cap on a $10 million notional.

5.50%

maximum funding cost, plus the premium

SOFR	Borrowing cost	Cap pays	Net annual cost
3.50%	$350,000	$0	**$350,000**
4.50%	$450,000	$0	**$450,000**
5.50%	$550,000	$0	**$550,000**
6.50%	$650,000	$100,000	**$550,000**
7.50%	$750,000	$200,000	**$550,000**

Below 5.50%, the bank keeps the benefit of lower rates.

Above 5.50%, the cap pays the difference, so costs stop rising.

Hypothetical, for illustration only. Assumes the borrowing rate equals SOFR; excludes the upfront premium.

SIDE BY SIDE

Swaps vs. caps and floors at a glance

	Swap	Cap or floor
What it does	Converts a floating rate to fixed (or fixed to floating)	Sets a ceiling (cap) or a minimum (floor) on a floating rate
Upfront cost	Typically none	An upfront premium, like an insurance payment
If rates move against you	You're protected; swap payments offset the change	You're protected beyond the cap or floor; the option pays the difference
If rates move in your favor	You give up the benefit; the rate stays locked	You keep the benefit; the option simply goes unused
Value over time	Rises or falls with rates; collateral may be required	The most the buyer can lose is the premium paid
Often considered when	Certainty is the top priority	Protection against a worst case matters, while keeping some upside

Two ways community banks use derivatives

Balance sheet hedging

Managing the bank's own rate risk

- Lock in the cost of short-term or floating-rate funding
- Reduce the rate risk of long-term fixed-rate loans or securities
- Protect income on floating-rate loans if rates fall
- Help stay within board-approved interest rate risk limits

Loan-level hedging

Giving commercial borrowers a fixed payment



- The bank makes a floating-rate loan, and the borrower swaps it to a fixed payment
- The bank enters an equal and opposite swap with a dealer, so its own rate risk stays neutral
- The borrower gets a long-term fixed payment; the bank keeps a floating-rate asset

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When might a derivative be considered?

If earnings suffer when rates RISE

Liability sensitive

Tools commonly used

- Pay-fixed swap on floating-rate or short-term funding
- Pay-fixed swap against long-term fixed-rate loans or securities
- Interest rate cap on funding costs

If earnings suffer when rates FALL

Asset sensitive

Tools commonly used

- Receive-fixed swap against floating-rate loans
- Interest rate floor on floating-rate loans
- Collar to protect a range at lower upfront cost

Not every bank needs a derivative. They are usually considered only after interest rate risk modeling identifies a specific exposure, and when on-balance-sheet strategies would be less effective or more costly.

Weighing the benefits and the trade-offs

Potential benefits

Targeted: Address a specific amount and time period

Fast: Adjust risk without selling assets or changing customer products

Flexible: Start today or in the future; hedge all or part of a balance

Efficient: Swaps usually require no upfront premium

Things to weigh

Lost upside: A hedge can cost money if rates move the other way

Liquidity: Value changes may require posting collateral

Counterparty risk: The other side must be able to perform

Accounting: Hedge accounting requires documentation and ongoing testing

Governance: Board policy, limits, expertise and regulatory requirements

Questions to ask before considering derivatives

1. What specific risk are we trying to reduce, and how large is it?
2. Could on-balance-sheet strategies address it just as well?
3. How would the hedge perform if rates move the “wrong” way?
4. Do we have the liquidity for collateral and the expertise to manage it?
5. How will it be accounted for and explained to the board and examiners?

What's typically involved

1. Board education
2. Board-approved policy and limits
3. Risk modeling and strategy analysis
4. Accounting and auditor review
5. Legal agreements and counterparty setup
6. Ongoing monitoring and ALCO reporting

Expectations come from your primary regulator and should fit the bank's size and complexity.

Glossary of key terms

Notional amount: Reference amount used to calculate payments; never exchanged

Collateral: Cash or securities posted to cover a contract's current value

SOFR: Secured Overnight Financing Rate, the main U.S. floating-rate benchmark

Mark-to-market: A contract's current market value

Swap rate: The fixed rate in a swap, based on expected future rates

Counterparty: The other party to the contract

Pay-fixed / receive-fixed: Which side of a swap a bank is on

ISDA agreement: The standard legal contract that governs derivative trades

Strike rate: The level at which a cap or floor starts to pay

Hedge accounting: Rules (ASC 815) that match a hedge with the item it protects

Premium: Upfront price paid to buy a cap, floor or other option

Eligible contract participant: Regulatory test a borrower must meet to enter a swap

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High Performing Bank Review

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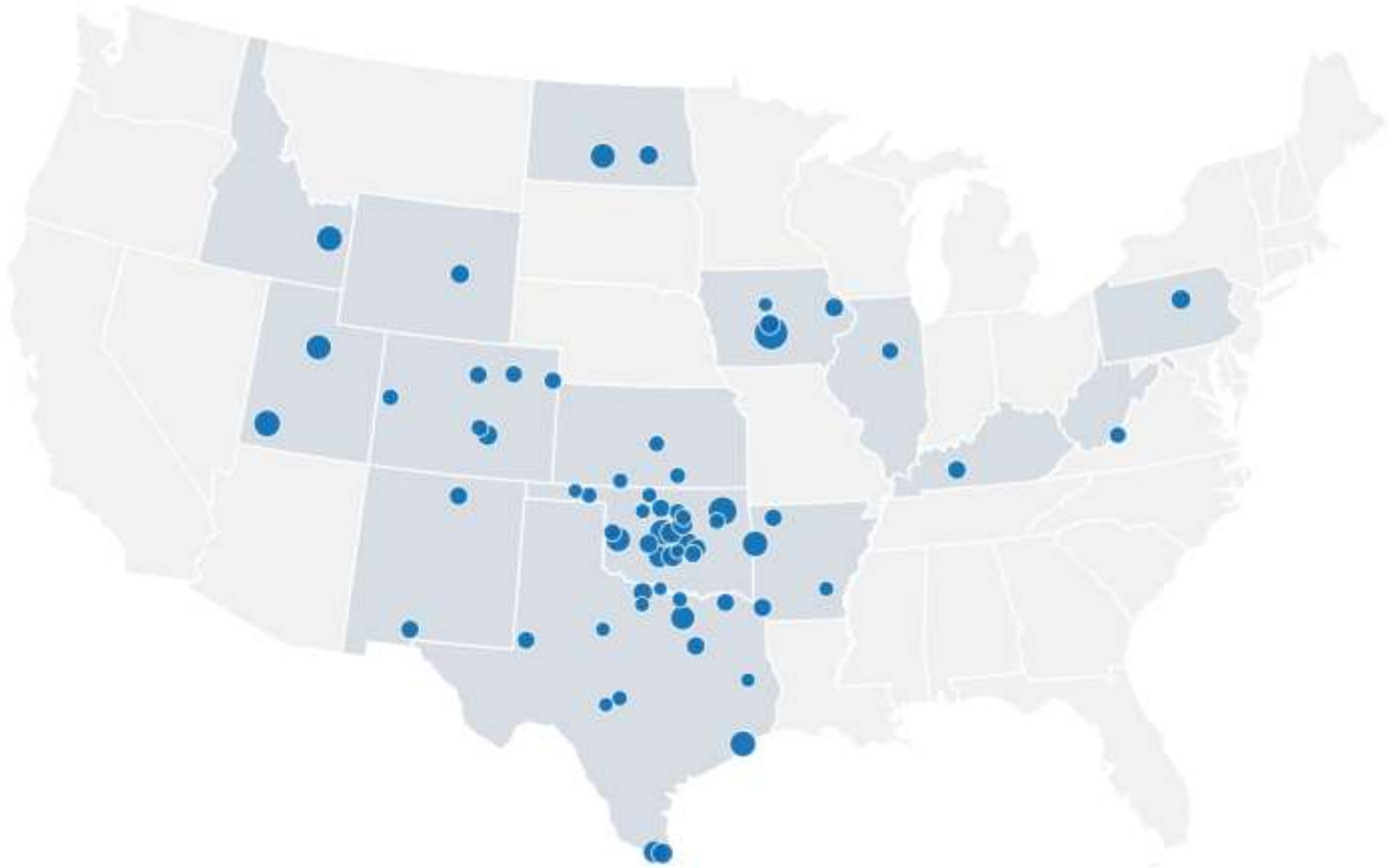
Who’s in the Room



Financial institution Dot size = total assets

66

Financial institutions in attendance

15 states

Oklahoma 23 · Texas 15 · Colorado 6 · Iowa 4 · 11 other states

$59.6B

Combined total assets across all 66 institutions

<$100MM–$7.8B

Range of total assets; the median institution is $394MM

Source: The Baker Group 2026 Oklahoma Seminar attendee list (Oct. 15–16, 2026); S&P Capital IQ Pro. One record per institution.

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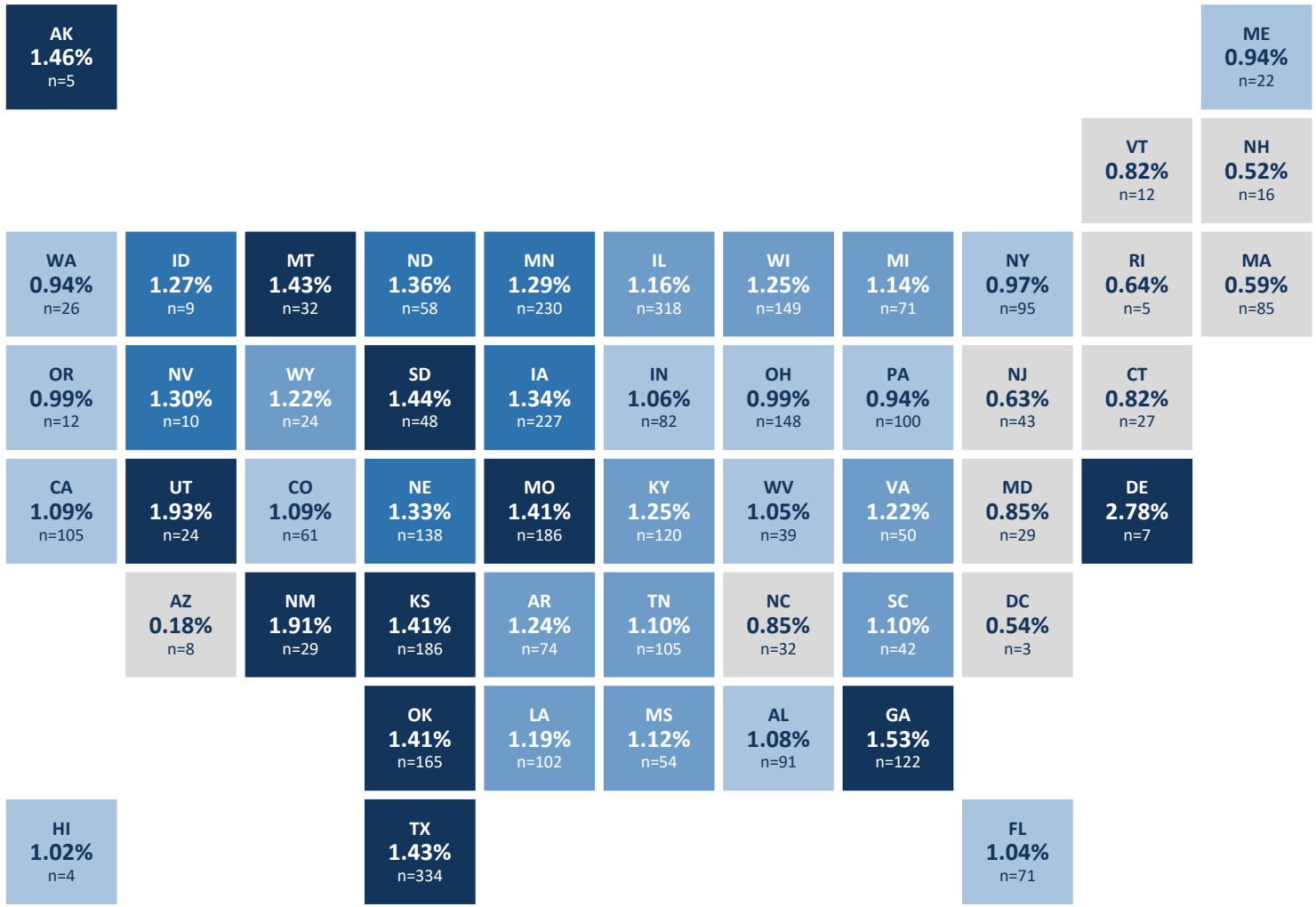
Where the Returns Are: Median ROAA by State

Community banks under $10B, 2Q 2026 annualized. U.S. median 1.21% across 4,040 banks. Each tile: median ROAA and number of banks.



MEDIAN ROAA, 2Q 2026

- Below 0.90%
- 0.90% – 1.09%
- 1.10% – 1.24%
- 1.25% – 1.39%
- 1.40% and above

HIGHEST (10+ BANKS)

UT 1.93% (24)
NM 1.91% (29)
GA 1.53% (122)
SD 1.44% (48)
MT 1.43% (32)

LOWEST (10+ BANKS)

NH 0.52% (16)
MA 0.59% (85)
NJ 0.63% (43)
VT 0.82% (12)
CT 0.82% (27)

Source: FFIEC Call Reports via The Baker Group's ratio engine; 4,040 community banks under $10B with 2Q 2026 data. Reported ROAA (not tax-adjusted), YTD annualized. Territories not shown.

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How We Found the High Performers

Not one good quarter. A three-and-a-half-year record, tax-adjusted so Subchapter S banks compete on equal footing.

3,610
Community banks under $10B analyzed

361
High performers: the top 10%

1.88%
Median tax-adjusted ROAA of the top 10% — vs. 0.99% for the middle 50%

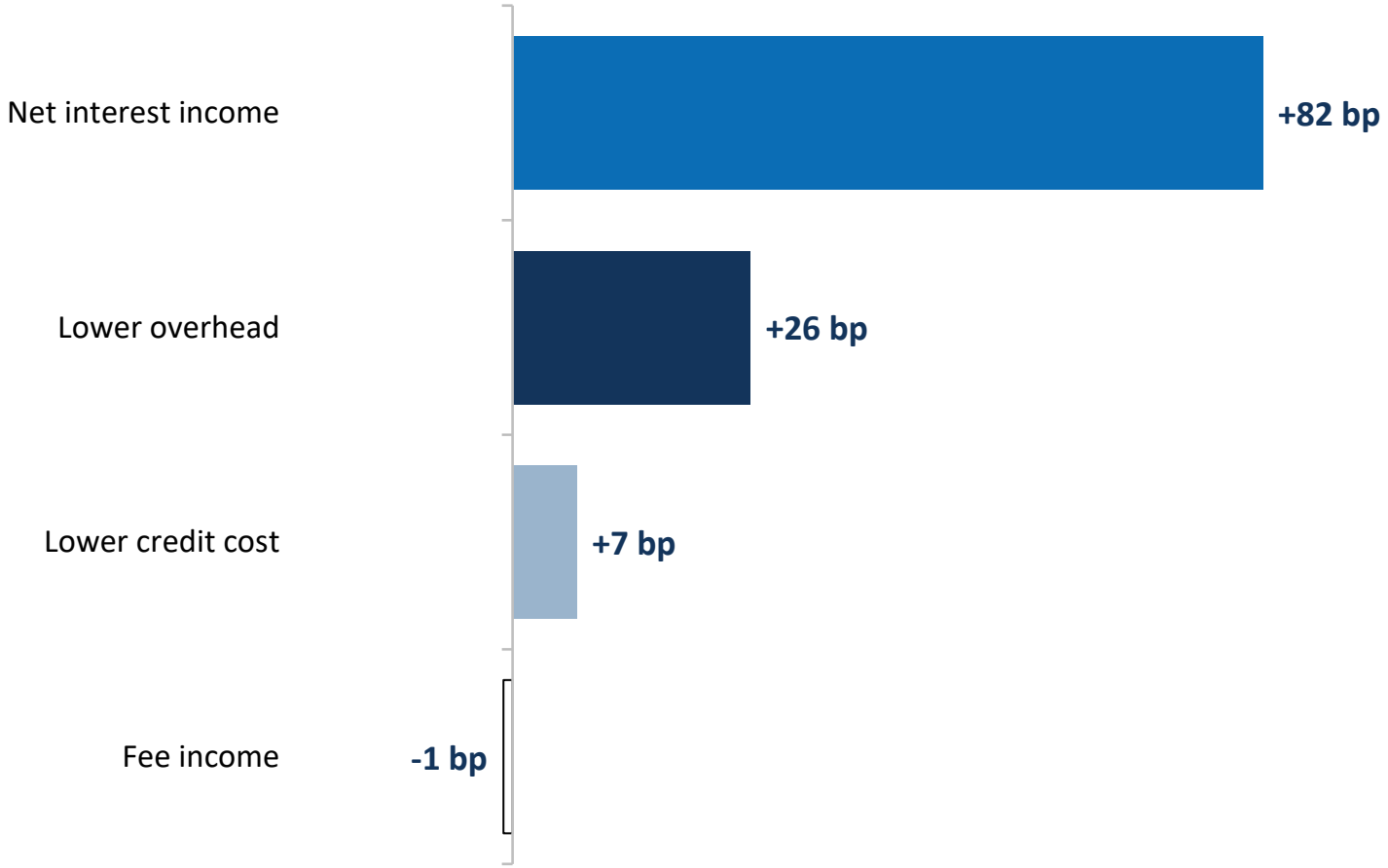
17.5%
Median ROE of the top 10% in 2Q 2026 — vs. 12.2% for the middle 50%

- **The score:** average return on average assets for full-year 2023, 2024, 2025 and 2Q 2026 (annualized), with S-corp income taxed at 21% using the UBPR method.
- **The universe:** banks under $10B with at least $50MM in assets, chartered before 2017, loans at least 25% of assets — specialty lenders and trust banks screened out.
- **The comparison:** Top 10% (361 banks) vs. the Middle 50% (1,806) and the Bottom 25% (902). Every number in this deck is a median unless noted.
- **The median size:** the median high performer has $410MM in assets

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

Where the Extra 117 Basis Points Come From

Pretax ROAA, Top 10% vs. Middle 50%, 2Q 2026 (mean, % of average assets): 2.61% vs. 1.44%.



70% of the advantage is margin

22% is overhead

6% is credit cost

0% is fee income

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. This slide uses means so the pieces add up; ~2 bp of securities gains and rounding not shown.

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What the Top 10% Do Differently

Top 10% vs. Middle 50%

1. **Win on the margin, not on fees**
   NII 4.47% vs. 3.60% of assets; fees identical at 0.42%

2. **Fund with free money**
   Noninterest-bearing 25.6% vs. 20.9% of deposits

3. **Don’t rent the balance sheet**
   63% use no FHLB advances vs. 45%

4. **Put the balance sheet to work in loans**
   Loan-to-deposit 86% vs. 82%; loans 73% vs. 70% of assets

5. **Get paid to lend**
   Loan yield 7.18% vs. 6.49% — with the same charge-offs

6. **Keep the loan book short**
   43% reprices within a year vs. 34%

7. **Be more productive, not cheaper**
   Revenue per FTE $381K vs. $294K; cost per FTE the same

8. **Run fewer, bigger offices**
   $90MM of assets per office vs. $84MM

9. **Buy bonds with discipline**
   Unrealized loss −3.2% vs. −5.3%; yield 3.56% vs. 3.09%

10. **Grow and build capital while doing it**
    Loans +24% vs. +21% since mid-2023; leverage 12.9% vs. 10.7%
    Higher retained earnings fund faster growth without thinning capital

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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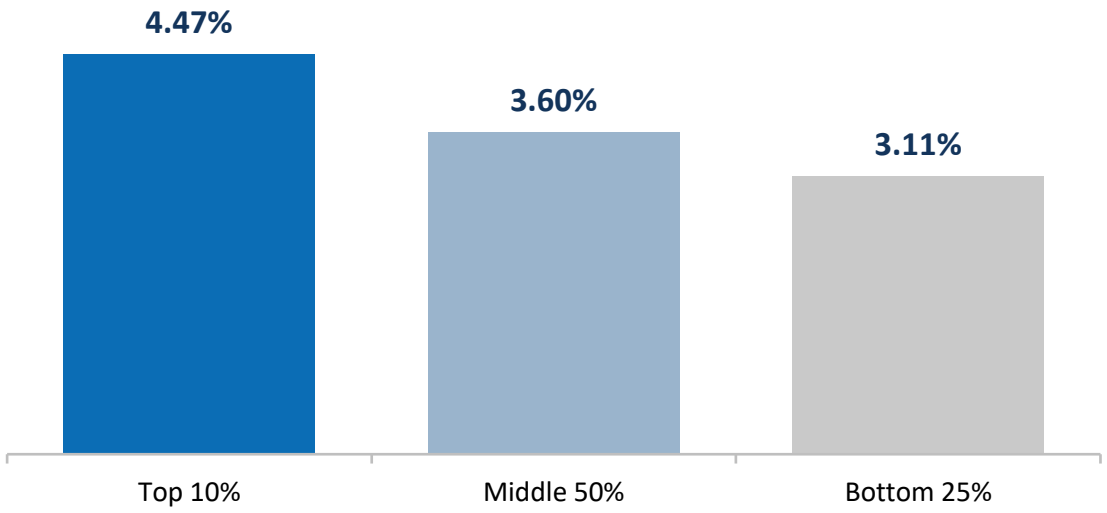
The Margin Story Starts With Funding

The top 10% earn 87 bp more net interest income on the same size balance sheet. Their deposit mix explains a big piece of it.

1 Win on the margin, not on fees

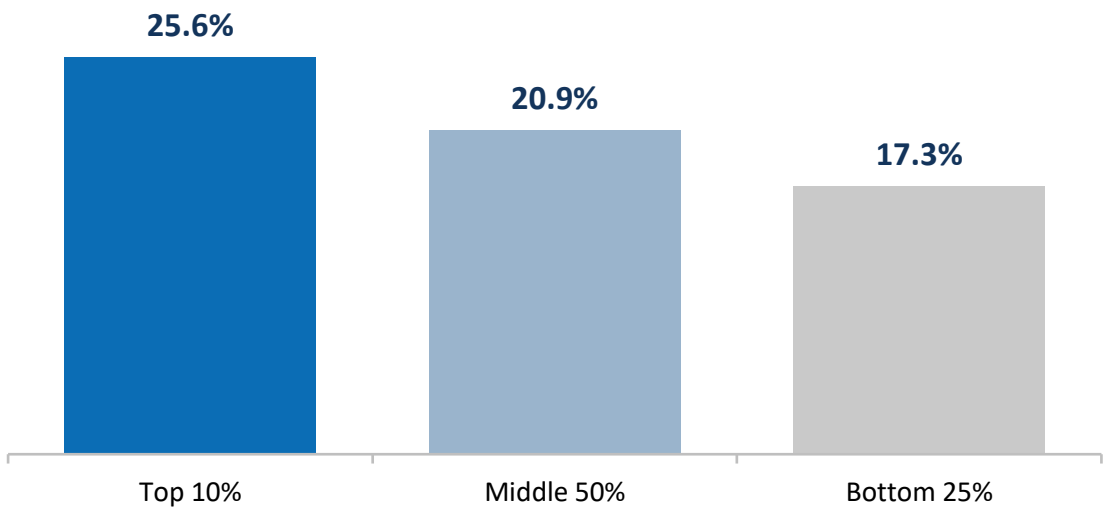
NET INTEREST INCOME, % OF AVERAGE ASSETS



- **Fee income:** 0.42% vs. 0.42%. Identical.
- **Interest income +70 bp,** interest expense −19 bp vs. the middle
- **NIM:** 4.73% vs. 3.82% vs. 3.30%

2 Fund with free money

NONINTEREST-BEARING DEPOSITS, % OF DEPOSITS



- **Cost of funds:** 1.49% vs. 1.70% vs. 1.79%
- **Less time money:** 16% of deposits vs. 18% vs. 19%
- **More MMDA, fewer jumbo CDs** than the bottom quartile

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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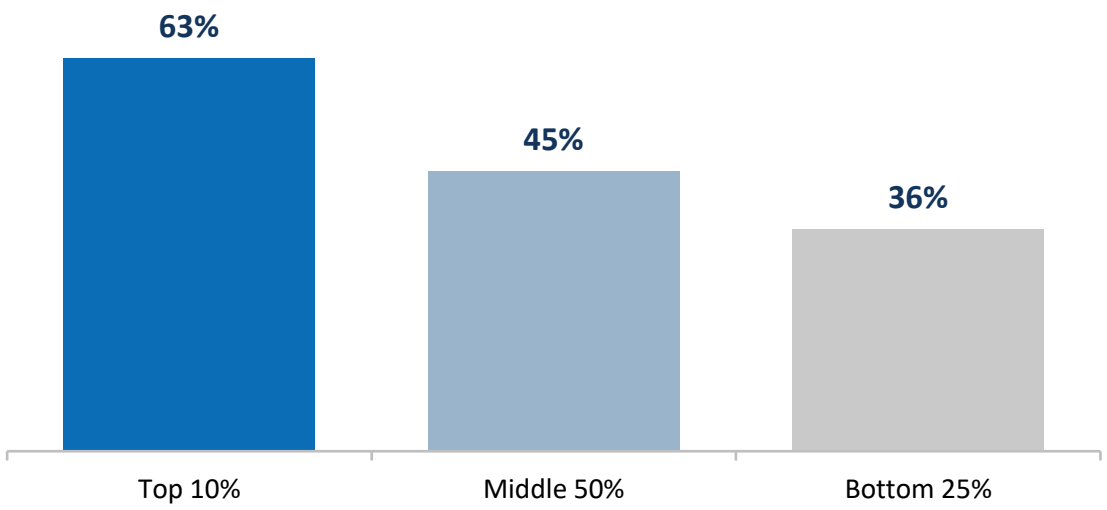
They Own Their Balance Sheet — and Lend It Out

High performers fund loans with deposits, not advances — and lend out more of the balance sheet.

3 Don’t rent the balance sheet

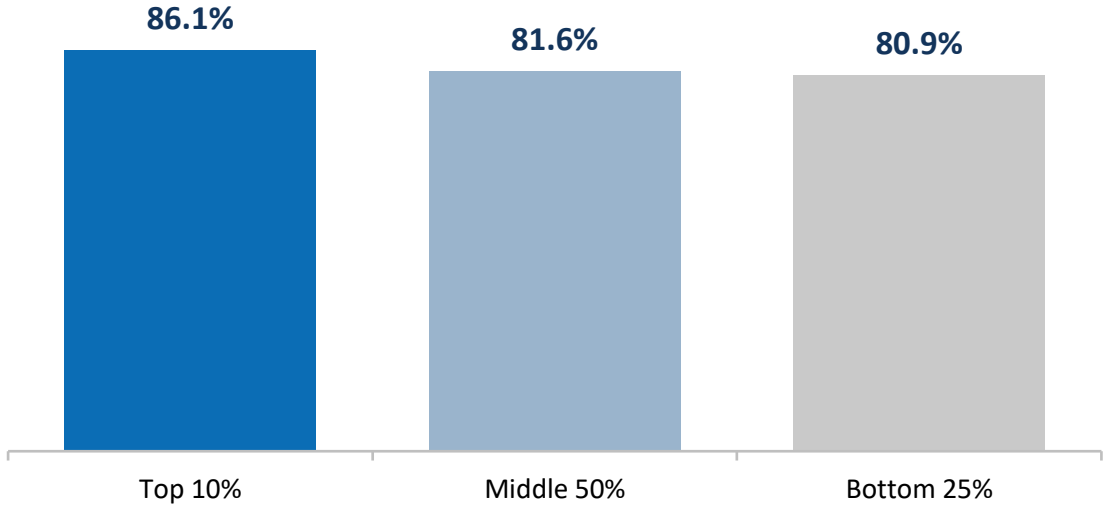
SHARE OF BANKS WITH NO FHLB ADVANCES



- **Wholesale funding:** 0.3% of assets vs. 2.2% vs. 4.2%
- **Half carry no borrowings at all** (51% vs. 35% vs. 30%)
- **Borrowings are a tool,** not a funding source

4 Put the balance sheet to work in loans

LOAN-TO-DEPOSIT RATIO



- **Securities:** 12.9% of assets vs. 18.3% vs. 18.5%
- **Interest-bearing cash:** 8.7% of assets vs. 5.0% — liquidity held as cash
- **Loans:** 72.7% of assets vs. 70.0%

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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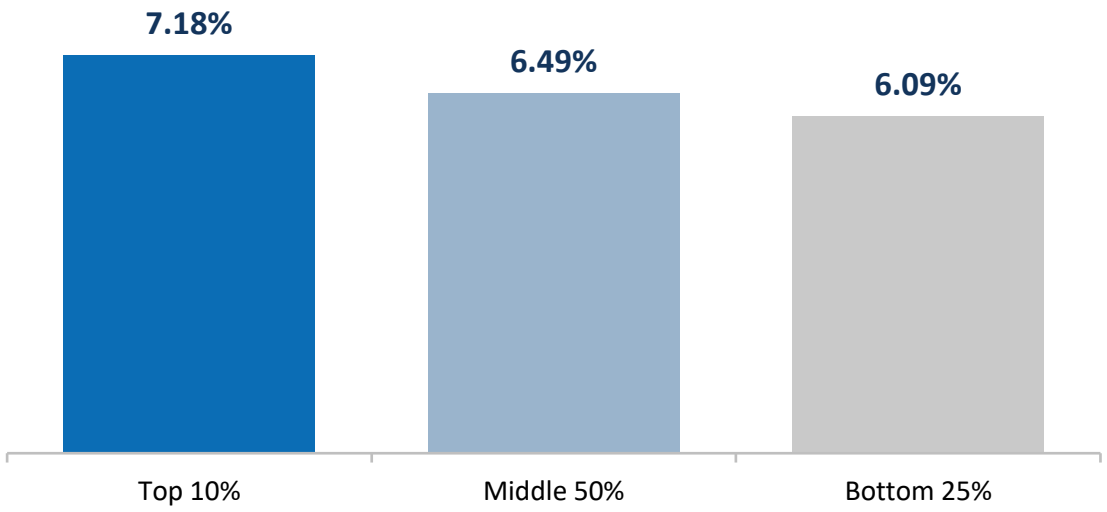
They Price for Yield and Keep It Short

Higher loan yields without higher charge-offs, and a loan book that reprices with the market.

5 Get paid to lend

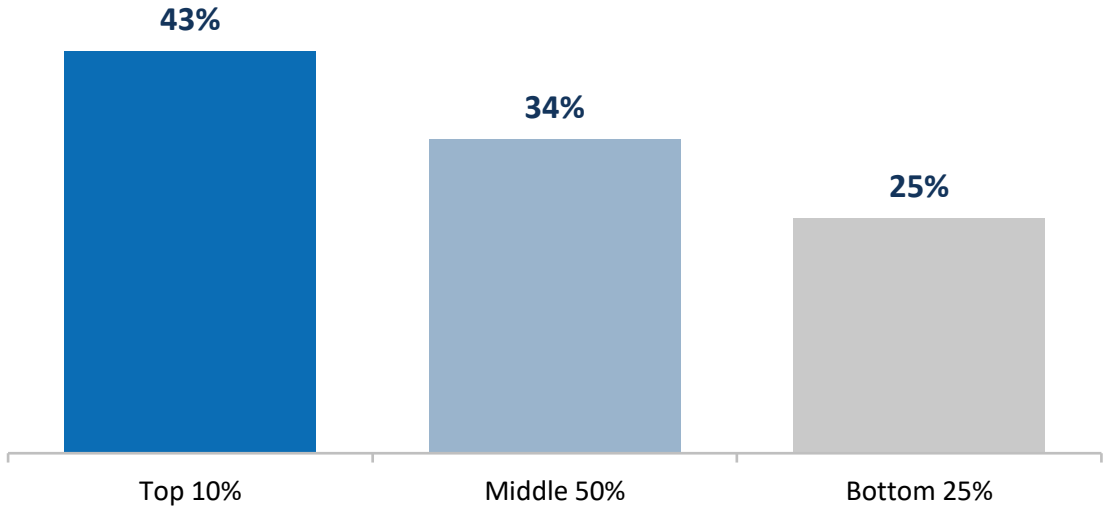
YIELD ON LOANS



- **Net charge-offs:** 0.01% vs. 0.01% — the same
- **+69 bp of loan yield** on the largest asset on the books
- **Less 1–4 family:** 26% of loans vs. 30% vs. 39%

6 Keep the loan book short

LOANS REPRICING OR MATURING WITHIN 1 YEAR



- **Beyond 5 years:** 8% vs. 16% vs. 29%
- **Trough NIM 2022–24:** 3.45% vs. 2.95% vs. 2.55%
- **Trade-off:** more asset-sensitive if the Fed reverses

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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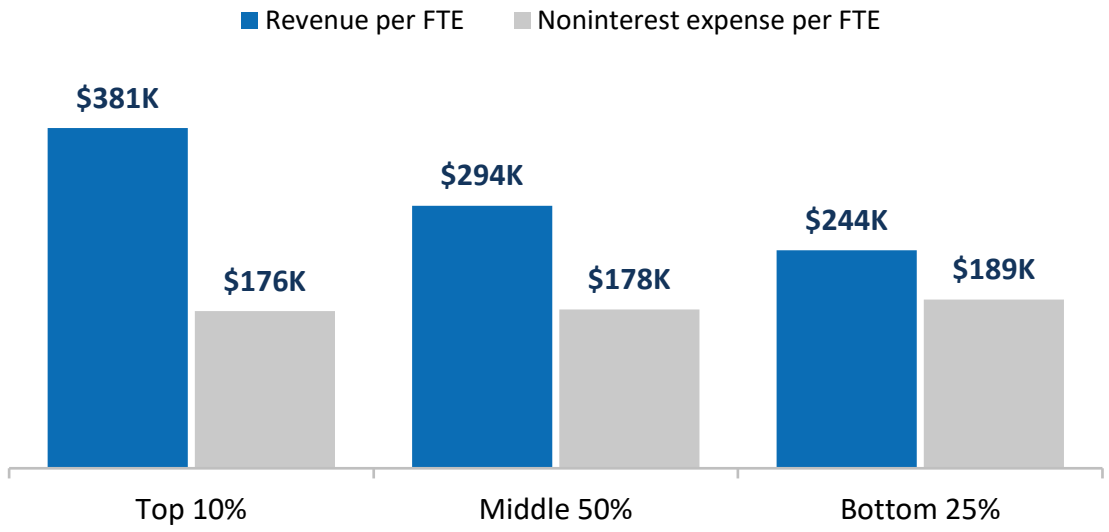
Leaner Means More Productive, Not Cheaper

High performers spend about the same per employee. Each employee just produces a lot more revenue.

7 Be more productive, not cheaper

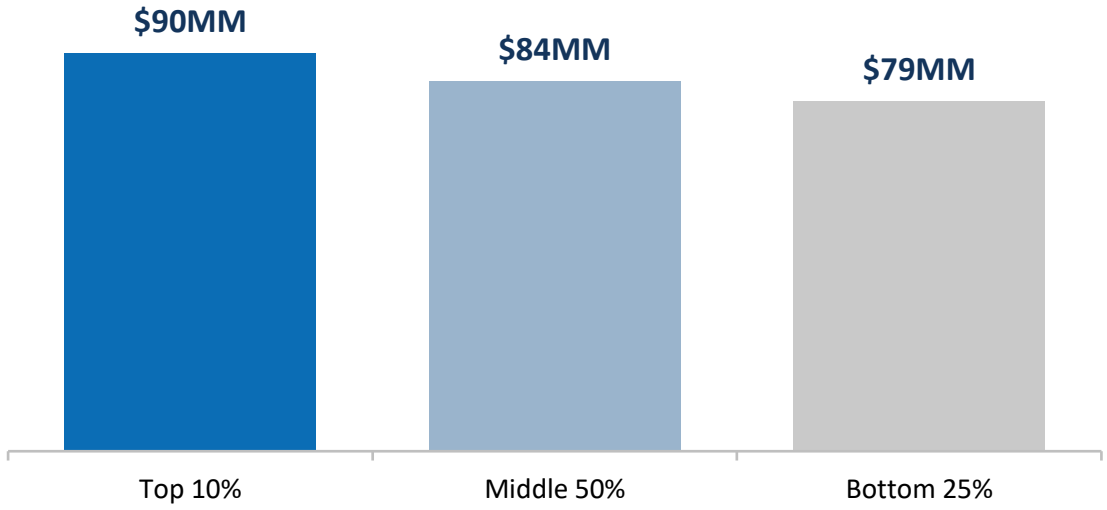
PER FULL-TIME EMPLOYEE, ANNUALIZED ($000)



- **Efficiency ratio:** 46% vs. 62% vs. 78%
- **Assets per FTE:** $7.9MM vs. $7.2MM vs. $7.1MM
- **Salaries:** 1.33% of assets vs. 1.43% — not lower pay, more output

8 Run fewer, bigger offices

ASSETS PER OFFICE ($MM)



- **Occupancy:** 0.21% of assets vs. 0.26% vs. 0.28%
- **Deposits per office:** $75MM vs. $72MM vs. $66MM
- **Median offices:** 4 vs. 5 — on the same size balance sheet

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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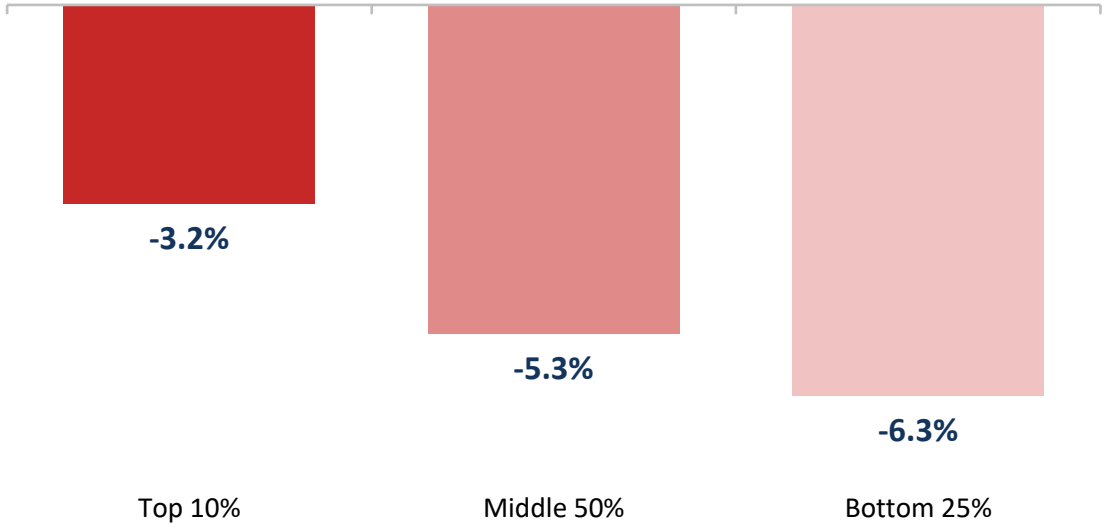
Disciplined Bond Buying, More Capital, Faster Growth

The payoff: smaller unrealized losses, higher portfolio yields, and the capital to keep growing.

9 Buy bonds with discipline

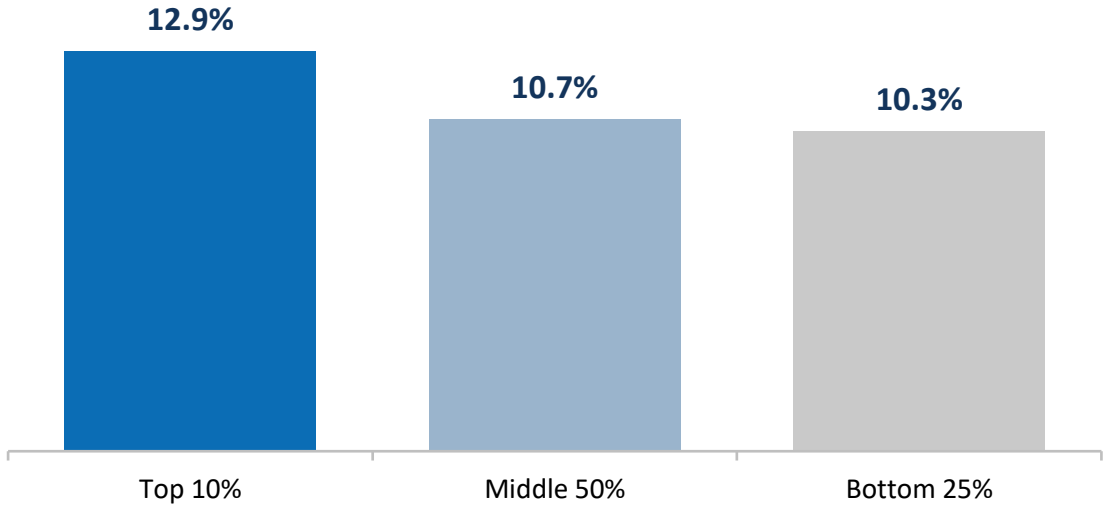
UNREALIZED GAIN/(LOSS), % OF AMORTIZED COST



- **Portfolio yield:** 3.56% vs. 3.09% vs. 2.86%
- **Fewer CMOs:** 47% hold any vs. 65% vs. 66%
- **Bought with discipline —** less locked in at 2020–21 lows

10 Grow — and build capital while doing it

TIER 1 LEVERAGE RATIO



- **Loan growth since 2Q 2023:** +24% vs. +21% vs. +12%
- **Deposit growth:** +16% vs. +13% vs. +6%
- **ROE:** 17.5% vs. 12.2% vs. 5.8% — capital funds the growth

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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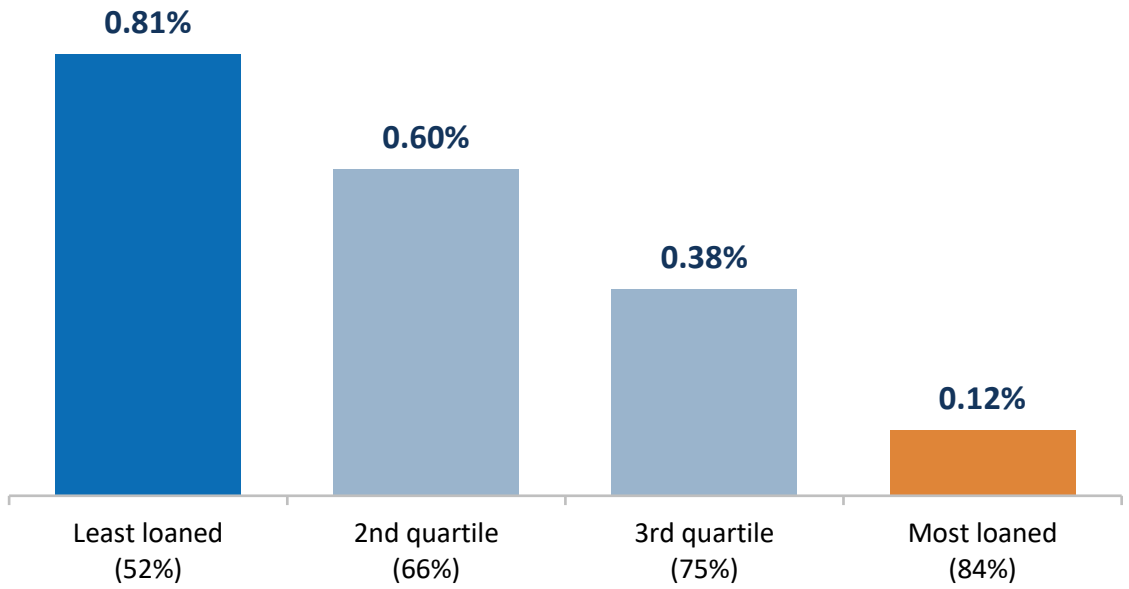
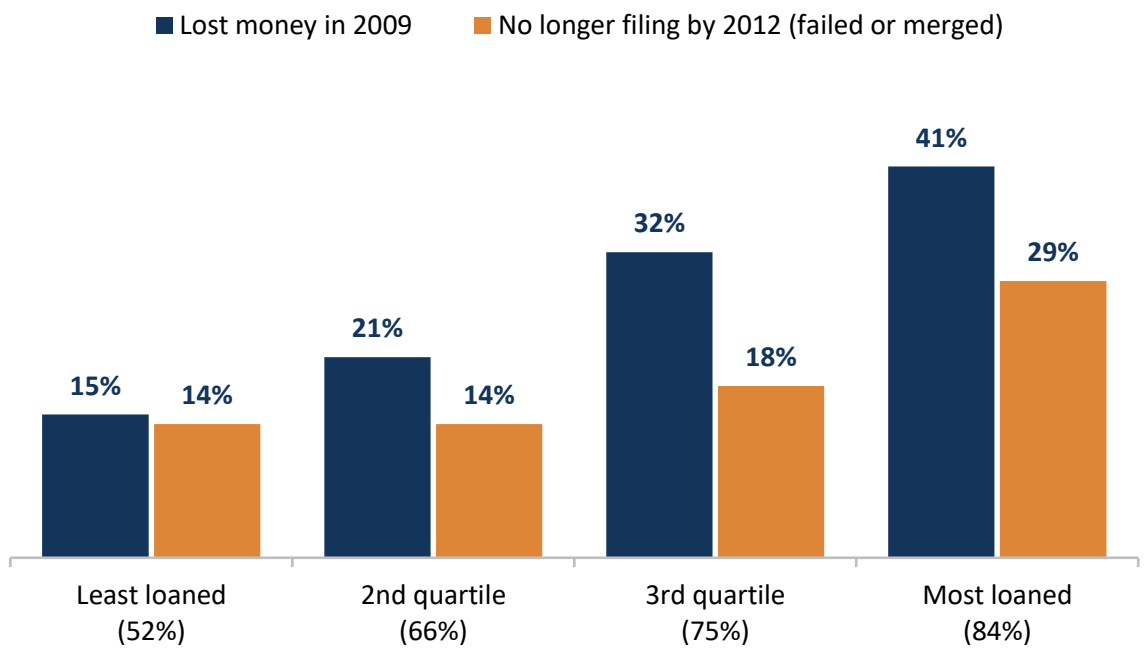
The Credit Cycle Caveat

Loaned-up has paid for fifteen years. Community banks grouped by loans-to-assets going into the 2008–09 crisis (4Q 2007).

RETURN ON AVERAGE ASSETS, 2009 (MEDIAN)



SHARE OF BANKS THAT…



- **Going in, they earned the same:** 2007 ROAA 0.93% for the most loaned vs. 1.05% for the least.
- **Coming out, they didn't:** 2010 net charge-offs 0.89% vs. 0.28%.

- **The most loaned-up quartile held** 7% of assets in bonds; the least held 35%.
- **Today's top 10% run an 86% loan-to-deposit ratio** with charge-offs near zero. The bond book is the earnings and liquidity left standing when that changes.

Source: FFIEC Call Reports via The Baker Group's ratio engine. 5,989 banks with $50MM–$10B in assets at 4Q 2007, grouped into quartiles by loans/assets. Medians. "No longer filing" includes mergers as well as failures.

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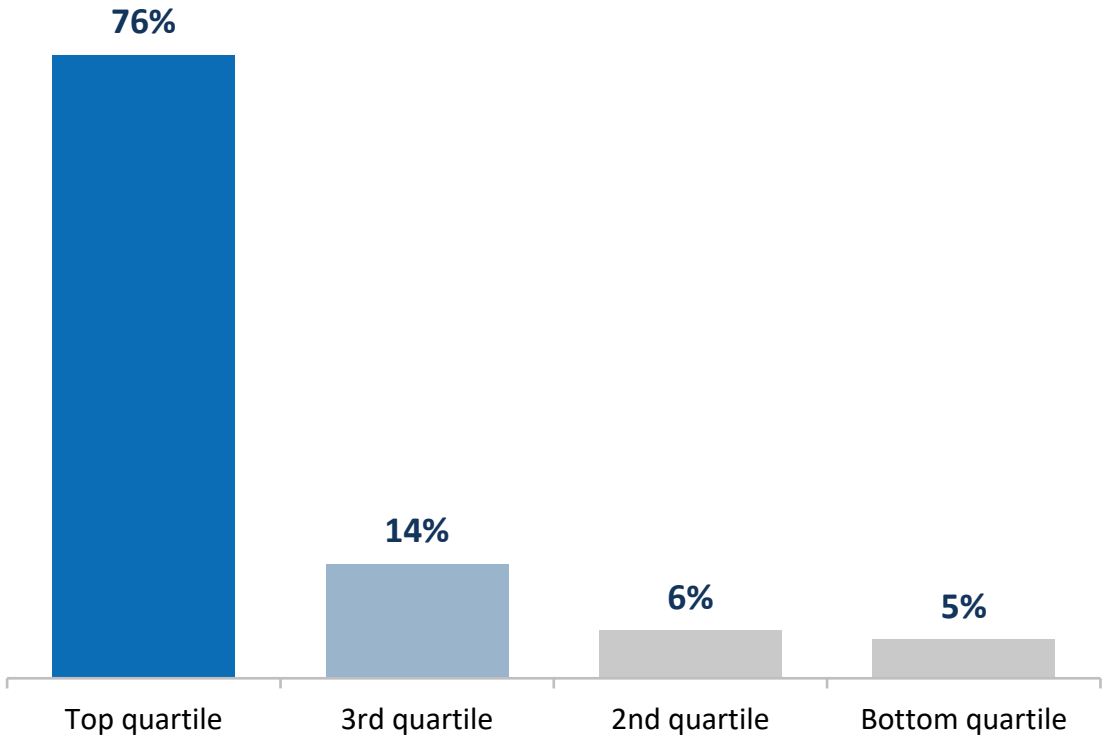
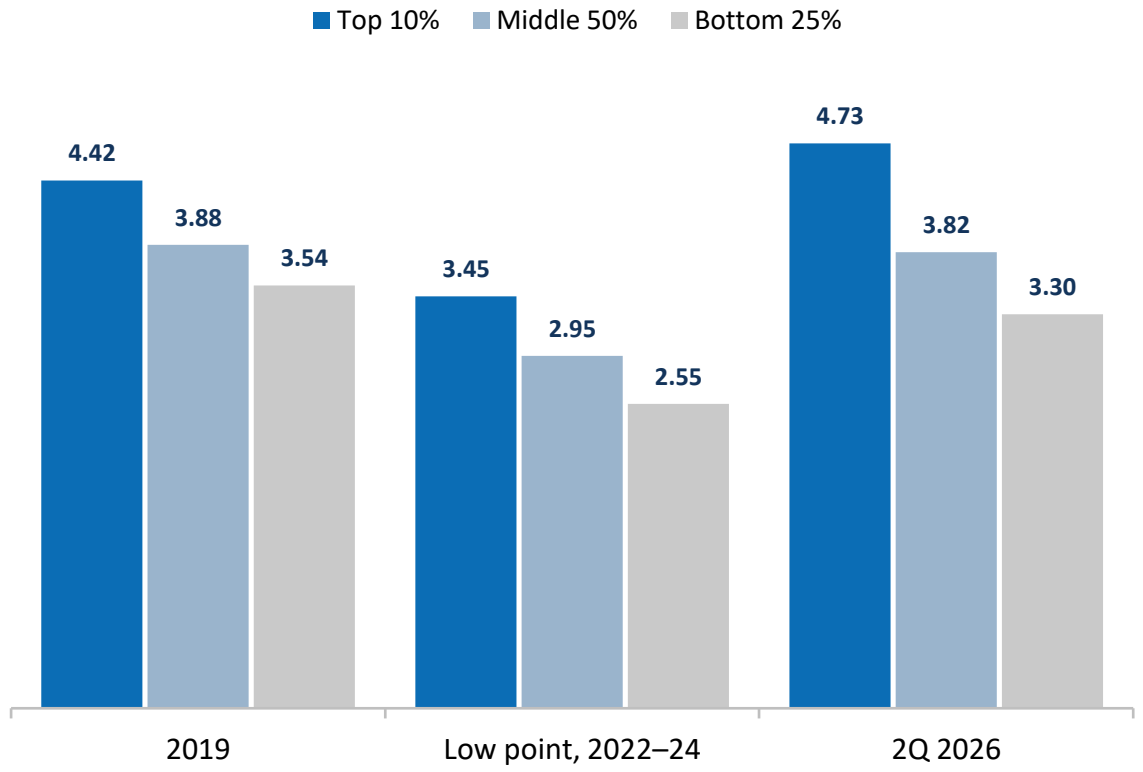
High Performance Is a Habit

90% of today's top 10% were in the top quartile in every one of the four periods we measured.

WHERE TODAY'S TOP 10% RANKED IN 2019



NET INTEREST MARGIN THROUGH THE CYCLE



Only 5% of today's bottom quartile were top-quartile in 2019. The gap is a decade of decisions — which means it can be closed one decision at a time.

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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Three Myths About High Performers

The most common explanations for the gap don't hold up in the data.

MYTH

"You have to be big."

Size doesn't decide it.

- Median high performer: $410MM — same as the middle
- Share of banks in the top 10% by size: $100–250MM 11% · $250–500MM 10% · $500MM–1B 11% · $1–10B 9%
- Only banks under $100MM lag (7%)

MYTH

"It's fee income."

Fees are identical.

- Noninterest income: 0.42% of assets vs. 0.42% for the middle 50%
- Fee income explains 0 bp of the 117 bp pretax gap
- The difference is on the balance sheet

MYTH

"They take more credit risk."

Credit costs are the same, so far.

- Net charge-offs: 0.01% vs. 0.01%
- Provision: 0.07% vs. 0.07% of assets (medians)
- Noncurrent loans slightly higher: 0.52% vs. 0.44% — worth watching, not the driver

And it isn't the tax status. 49% of the top 10% are Subchapter S (vs. 37%) — but we taxed their income at 21% before ranking.

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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Where Does Your Institution Rank? Scorecard

Fill in the right-hand column on the plane home. Medians, 2Q 2026.

Metric	Top 10%	Middle 50%	Your institution
Net interest income, % of avg assets	**4.47%**	3.60%	
Noninterest-bearing deposits, % of deposits	**25.6%**	20.9%	
Cost of funds	**1.49%**	1.70%	
Wholesale funding, % of assets	**0.3%**	2.2%	
Loan-to-deposit ratio	**86%**	82%	
Yield on loans	**7.18%**	6.49%	
Loans repricing within 1 year	**43%**	34%	
Revenue per FTE (annualized)	**$381K**	$294K	
Efficiency ratio	**46%**	62%	
Assets per office	**$90MM**	$84MM	
Tier 1 leverage ratio	**12.9%**	10.7%	

Source: FFIEC Call Reports via The Baker Group's ratio engine. 3,610 community banks under $10B; Top 10% = 361 banks ranked on tax-adjusted ROAA averaged over YE 2023, 2024, 2025 and 2Q 2026. Medians.

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Thank You!

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