# Liquidity and Asset-Liability Management

Managing Cash and Liquidity for Native CDFI's

OWEESTA Corporation

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6th Annual Native CDFI Capital Access Convening
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# Trainer Introductions

- Krystal Langholz, Chief Operating Officer
- Florence Ludka, Chief Financial Officer
- Mikeala Ludka, Lending Assistant




OWEESTA Corporation

Jamie

# Menti Activity

# What is Liquidity?

Liquidity measures the extent to which an organization has cash, access to cash, or assets that can be quickly converted to cash, to meet immediate and short-term obligations.

# Liquid Assets

Assets that can be quickly converted to cash to meet immediate and short-term obligations:

Cash

Cash Equivalents

Marketable Securities

# Mural Activity

# Restrictions and Limitations on Assets Example

| Assets | March 2021 | March 2020 | Change |
|---|---|---|---|
| Current Assets | | | |
| Cash for Operations (Unrestricted Cash) | $3,711,379 | $1,936,614 | $1,774,765 |
| Cash for Grant and Contract Deliverables | 2,666,389 | - | 2,666,389 |
| Cash for Lending | 8,033,083 | - | 8,033,083 |
| Interest and other receivables | 70,021 | 41,311 | 28,710 |
| Government Grants Receivable | 625,000 | 1,146,333 | (521,333) |
| Investments for Operations | - | - | - |
| Investments for Grant & Contract Deliverables | - | 1,333,142 | (1,333,142) |
| Investments for Lending | 6,212,786 | 4,866,764 | 1,346,022 |
| Investments for Cash LLR | 1,000,000 | 1,000,000 | 0 |
| Prepaid Expenses | 8,063 | 8,731 | (669) |
| Total Current Assets | $22,326,721 | $10,332,895 | $11,993,826 |

# Liquidity for CDFI's

- Liquidity for a CDFI refers to the ability of the organization to meet demands for funds.
- Ensure the organization maintains sufficient cash and liquid assets
- Ensure adequate liquidity reserves in case of unexpected events;
- Ensure adequate liquidity for projected growth; and
- Fund assets and obligations in the most cost-effective way without unduly risking revenue potential

# Liquidity Management

Involves analysis and monitoring of the size and timing of cash inflows and outflows

# Liquidity Management Policy

- What position in the organization is responsible
- What is the general methodology and how will it be monitored and how frequently
- The level of risk the organization is prepared to take in minimizing cash and at the same time enhancing profitability
- Establish minimums and maximums for total cash assets
- How and when are decisions about liquidity made
- Which assets are considered liquid
- What are acceptable reasons or scenarios for accessing a line of credit

# Example

Ponderosa CDFI is 98% deployed, has a loan pipeline of $1.2MM, and no investment pipeline.  Ponderosa CDFI has no available lending capital to lend out, and no prospects for additional lending capital any time soon.

What happened with this CDFI?
What should they do?

# CDFI Liquidity Ratios

- Operating Liquidity Ratio

| | | | |
|---|---|---|---|
| **Unrestricted Cash & Cash Equivalents** | + | **Cash & Cash Equivalents Restricted for Operations** | X12 |
| Total Expenses for Prior Fiscal Year | - | Non-cash Expenses | >3 months |

- Current Ratio

| | | | |
|---|---|---|---|
| **Current Assets** | / | **Current Liabilities** | Ratio >1.2 |

- Quick Ratio

| | | | |
|---|---|---|---|
| **Liquid Assets** | + | **Current Loans Receivable** | |
| | Current Liabilities | | Ratio>1.0 |

- Capital Liquidity Ratio

| | | | |
|---|---|---|---|
| **Liquid Assets** | + | **Specific % of Current Loans Receivable** | |
| | Current Investor Notes Payable | | Ratio >1.0 |

# Cash Flow Projections

Detailed and realistic, capturing all sources and uses of liquidity

Updated and reviewed on a regular basis (frequency is dependent on a CDFI's respective cash flow activity).

Developed with information gathered from the following departments:

- Lending: Information regarding projected loan repayment schedules and loan disbursement schedules, including renewed loans and committed but undrawn loan facilities.
- Funding: Projected outflows related to maturing investor debt liabilities, plus undrawn debt liability commitments, including available funding lines of credit.
- Development: New donations, grants or other funding sources.
- Accounting/Finance: Other cash commitments and important payables, inclusive of any new high-dollar capital expenditures such as purchase of a building, or new IT equipment.
- Program Teams: Other program-related cash and expenditure commitments (e.g., training, conferences, pass-through grants)

Back-tested on a regular basis to understand if assumptions (such as the dollar amount of commitments funded) were correct.

# Asset-Liability Management (ALM)

ALM is the process of planning, organizing, and controlling asset and liability volumes, maturities, rates and yields in order to minimize interest rate risk and maintain an acceptable profitability level.

# The objective of ALM

Maintain and match the terms of assets in order to reduce interest rate risk while maximizing profitability in the terms of rate sensitive assets (those assets that will move in search of the most competitive interest rates).

# Example:

A housing focused CDFI wants to provide a 30-year mortgage product for 4%. It has a blend of equity and investor capital. Most of its loan fund currently has access to investor capital for a term of 5-7 years and equity.

What would you want to know to decide if it should expose itself to the risk of the 30-year mortgage product?

# Interest Rate Risk

The risk is the changes that may occur in the current market interest rates and how they adversely impact the organizations financial performance.

# Example:

Due to a pandemic many CDFI's were forced to adjust interest rates and give other concessions on loans receivable to avoid large portfolio delinquencies and write offs. But many investments remained concentrated in fixed-rate investments.  This scenario can cause financial performance to become impaired because CDFI's cannot adjust earned interest income upward fast enough as the cost of funds increases or remains the same.

# Breakout Room Activity

# ALM Monitoring

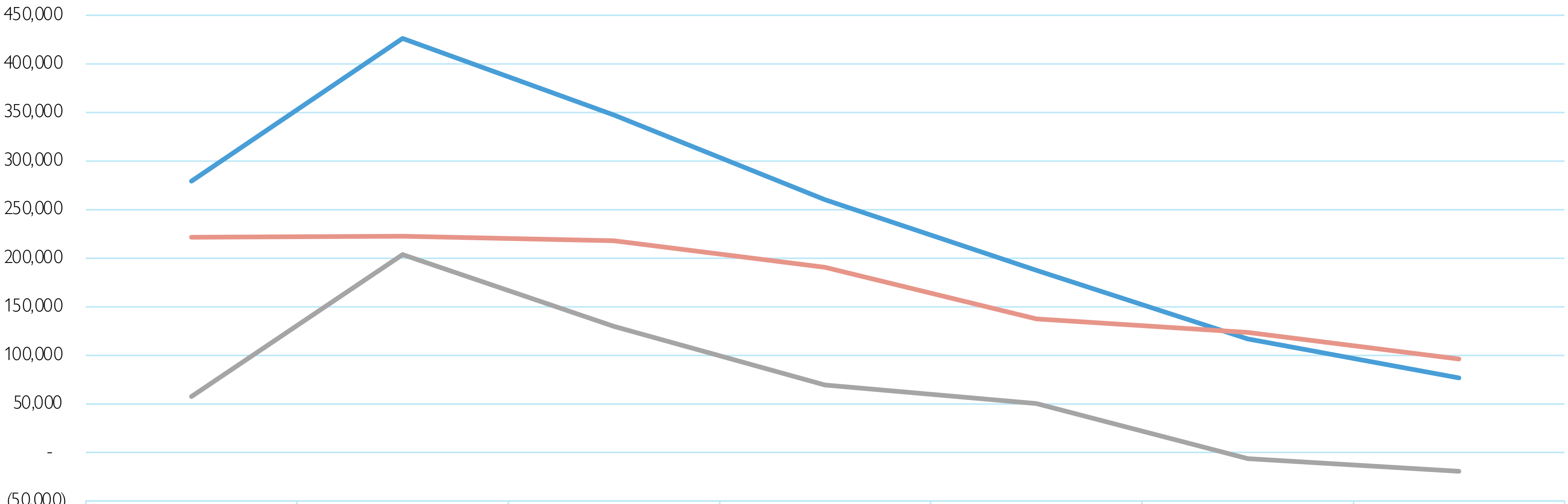
- Sensitivity Analysis
- Waterfall Analysis
- Interest Rate Sensitivity Analysis

# ALM Policy

- Who is responsible for ALM
- How often the ALM position will be analyzed and discussed
- What are the acceptable parameters or ranges for ALM ratios or indicators
- Short and long-term minimum capital or equity/total assets goal ratios.
- The maximum percentage of assets to be held by any one client, in different types of loans and investments
- The maximum amount in fixed rate investments and loans with a maturity greater than one year
- The maximum amount invested in fixed assets
- The desired diversification to eliminate potential concentration risk (having too much in any one loan type or sector or with any one client)
- Maximum maturities for all types of loans and investments
- Establishment of fixed or variable interest rate loans and deposits
- Pricing strategies for loans products based on the actual costs to offer the products and what the local market will bear

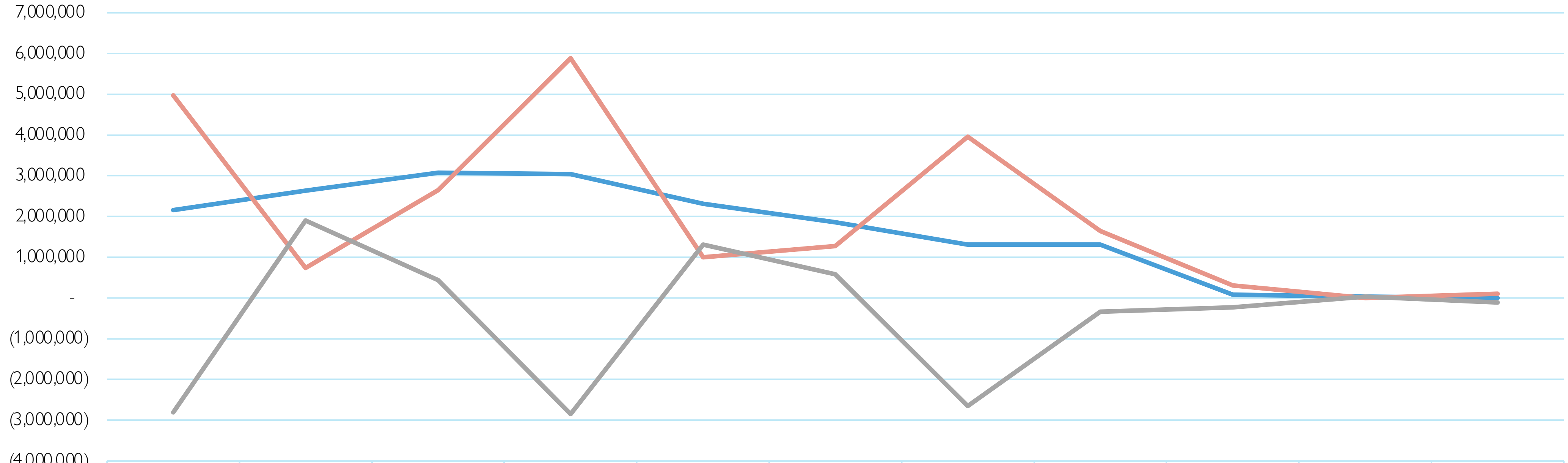
# Interest Payment Cash Flow Example

Interest Payment Cash Flow




| | 6/30/2021 | 6/30/2022 | 6/30/2023 | 6/30/2024 | 6/30/2025 | 6/30/2026 | Future |
|---|---|---|---|---|---|---|---|
| Incoming | 279,220 | 426,168 | 347,360 | 260,012 | 187,292 | 116,917 | 76,676 |
| Outgoing | 221,716 | 222,539 | 217,907 | 190,551 | 137,258 | 123,366 | 96,129 |
| Net | 57,503 | 203,629 | 129,453 | 69,461 | 50,035 | (6,449) | (19,454) |

# Principle Payment Cash Flow Example




| | 6/30/2021 | 6/30/2022 | 6/30/2023 | 6/30/2024 | 6/30/2025 | 6/30/2026 | 6/30/2027 | 6/30/2028 | 6/30/2029 | 6/30/2030 | Future |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Incoming | 2,157,853 | 2,638,242 | 3,074,184 | 3,035,311 | 2,309,946 | 1,858,227 | 1,310,781 | 1,311,257 | 76,415 | 38,390 | - |
| Outgoing | 4,968,750 | 736,796 | 2,640,868 | 5,883,963 | 995,061 | 1,276,219 | 3,962,382 | 1,643,568 | 310,394 | - | 105,000 |
| Net | (2,810,897) | 1,901,447 | 433,316 | (2,848,652) | 1,314,886 | 582,008 | (2,651,601) | (332,311) | (233,979) | 38,390 | (105,000) |

# Summary

- Liquidity management, ensuring that the institution maintains sufficient cash plus liquid assets to meet disbursement demands and pay expenses, is essential for loan funds.

- ALM, the process of planning, organizing, and controlling asset and liability volumes, maturities, rates, and yields in order to minimize interest rate risk and maintain an acceptable profitability level, is another key component.

# Questions

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