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Our Mission

The mission of the New Mexico Bankers Association (NMBA) is to serve member bank needs by acting as New Mexico banking's representative to government, the public, and the industry; providing resources, education and information to enhance the opportunities for success in banking; promoting unity within the industry on common issues; and seeking to improve the regulatory climate to the end that banks can profitably compete in the providing of financial and related products and services.

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PRESIDENT'S MESSAGE

DAVID HOCKMUTH

PRESIDENT
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The ability to help people is the best part of banking for me. I have the honor of helping customers with one of the most profoundly important aspects of their respective lives: money.

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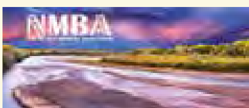

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AN INTERVIEW WITH NEW NMBA PRESIDENT DAVID HOCKMUTH

How did you get started in banking?
I started my banking practice with J.P. Morgan in New York. My full-time work for Morgan ran concurrently with my full-time studies at NYU. I was assigned to the American Depository Receipts Desk, which offered customers a way to purchase stocks in overseas companies that were otherwise unavailable to investors through U.S. stock exchanges. I began working on Wall Street to support my academic pursuits. I didn't have the intention of becoming a banker per se. Initially, I viewed banking as a means to an end. It turned out that I was pretty good at it. I frequently ask bankers to share their career goals with me. I find that many bankers do not set out to become bankers but discover the potential to have a highly fulfilling career in banking.

After living, studying and working in New York for seven years, I returned to New Mexico and was hired at United New Mexico Bank, which transitioned into Norwest Bank, which ultimately became Wells Fargo.

My career in banking began a mere thirty-seven years ago.

What has been the best part of being in the banking business?
The ability to help people is the best part of banking for me. I have the honor of helping customers with one of the most profoundly important aspects of their respective lives: money. I have never forgotten Mr. Micawber's advice since I first encountered it: "Annual income twenty pounds, annual expenditure nineteen pounds nineteen and six, result happiness. Annual income twenty pounds, annual expenditure twenty pounds ought and six, result misery." Money pays for all of the things we need and want. When money is managed well, it can be liberating and empowering. When it is managed poorly, it can become a source of unnecessary pressure and great distress. Money can impact whether or not we each get to pursue happiness. It can create security in one's life. The lack of it can result in abject poverty and unnecessary suffering. Acquiring and saving money can be challenging, and managing it can be complex. Helping people successfully manage their money has a profound impact on their lives which lends (pun intended) a certain nobility to our profession – our understanding of money obliges us to help our customers succeed financially.

What changes do you foresee in our industry and New Mexico in the next several years?
Whatever the changes to come, be assured that they will continuously arrive and always be early. Five years ago, during conferences and meetings, I suggested to bankers that technology would change our industry dramatically and that its pace would be faster and more comprehensive than all of the developments in the preceding

twenty years. My prediction was understated. Simple service transactions are migrating to mobile devices at fleet velocity. We are training bankers more comprehensively and quicker than those of yesteryear as a direct result of technological advancements.

Wherever bankers are situated in the world, including New Mexico, we need to be prepared to advise our customers about myriad options capable of making profound improvements in their personal economies. The opportunities for bankers to meet the challenges and excel on behalf of clients are thrilling to me. Just now, I'm thinking of the days of the abacus, the oldest calculating tool aside from fingers; the banker's first calculator. I imagine the conversations about money two thousand years ago employing an abacus, and then I contemplate a given conversation with a banker starting their career today. Next, I envision a conversation between a customer and a banker five years from now. That banker will have a BIG story to tell about the journey they and their clients have traveled.

Who has had the greatest influence on your career and why?

My wife Cassandra and my two brothers, Donald and Andrew, have had the greatest influence on my career. We are all bankers. Cassandra has helped me to be a better banker. She is the most empathetic banker I know and the most encouraging, especially when times are tough. She has taught me much about loyalty and courage. My brother Donald is the most directly responsible for my career in banking. What did I know as a seventeen-year-old kid just beginning in banking? Donald had already begun his journey into global finance and spoke to me about the merits of the profession. He compelled me to apply at Morgan, and we have been helping each other improve at banking for a long time. What a run. We lost our brother, Andrew, earlier this year. Andrew started his career as an actor in Los Angeles before returning to New Mexico to embark on a banking career. I compelled him to apply to Wells Fargo. Andrew was the most versatile banker amongst us, having worked in the regional, commercial and investment aspects of banking. He was one of my best men and remains my wingman.

I have also been fortunate to know many extraordinary leaders and colleagues throughout my career. Every fellow employee influences me because we are linked in this noble profession dedicated to helping our customers.

Do you have any advice for young bankers?

I love asking new bankers to recall when they were younger and share with me what they wanted to be when they grew up. Some of the proverbial responses are lawyer, doctor, nurse, athlete, policeman, firefighter, soldier, teacher, flight attendant, architect, engineer, scientist, physical therapist, pharmacist, rancher, farmer, veterinarian, computer programmer, politician, business person, musician, artist, etc. – the list goes on and on. A long time ago, my father advised me to use banking to my best advantage to learn, grow, and help others. I share this same advice with young bankers I meet today. Banking is one of the last great apprenticeships. You learn the job along the way, and you get better over time. The bank provides training and education throughout one's career, and there is no end to the learning process because banking always evolves.

Some bankers utilize a career in banking to follow other career goals. Banking has launched numerous careers outside of the financial industry. I know people from all walks of life (including a Jesuit priest) who began their careers in banking and went on to other jobs to fulfill their ultimate career goals.

Many of us have remained bankers.

When bankers tell me what they wanted to be when they grew up, I always tie their responses back to the people they serve. If you are a banker long enough, you will invariably meet people engaged in many of the various careers imagined by all of the bankers I have queried. In many ways, a career as a banker fulfills a deep curiosity about one's fellow human beings and their respective lives. Early in my career, I had the privilege of assisting my customer, an ichthyologist, obtain a loan. I had no idea what type of work an ichthyologist performed, but I found out and was fascinated. After all, it's not every day that you meet someone who knows everything there is to know about fish.

Tell us about your family.

Cassandra and I became grandparents in March of this year when we were blessed with the arrival of Saylor Rae. Our daughter Alleyne and son-in-law Ralf are proud parents who are mustering out of the United States Navy, where Ralf has served for the past five years. Ralf is continuing his education to become a physician's assistant. Alleyne is a very successful esthetician. Our son Kevin is a high school senior full of hope and promise. I have a tendency to spoil my family when I can, but recently I forewarned them: Saylor is now number one.

What are your interests outside of banking?

Faith, family, community, work, health, music, art, food, travel, adventures, reading and writing. ■

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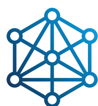

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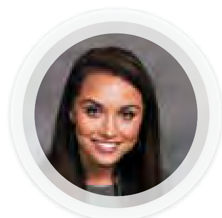

To learn more about BHG, Please Contact:

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BHG BANK NETWORK

EXECUTIVE VICE PRESIDENT'S MESSAGE

JOHN W. ANDERSON
EXECUTIVE VICE PRESIDENT
NEW MEXICO BANKERS ASSOCIATION

The theme for the convention was "Top Gun – Feel the Need . . . The Need to Succeed". Thanks to Jay Jenkins, we were lucky enough to have an actual Top Gun pilot as our keynote speaker.

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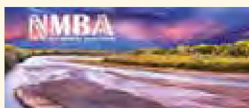

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NMBAs 110TH ANNUAL CONVENTION

The New Mexico Bankers Association 110th Annual Convention was a huge success. A special thanks to all who attended the convention September 15–16 at Buffalo Thunder Resort and Casino. The event began with an opening cocktail party and a vendor's event. I want to personally thank our vendors and sponsors for their support and generosity.

The education sessions were incredibly informative. Pete Trevisani, owner and president of the New Mexico United Soccer Club, discussed his inspiration for starting the team, the early days of being a gritty startup, the unbelievable support from the state, the success of the first season, the togetherness that helped the team survive 2020 and COVID-19, and what the future holds. All I can say is buy your season tickets now.

Brooke Ybarra, Vice President, Innovation Strategy, American Bankers Association, provided a framework for understanding various digital assets, including traditional cryptocurrency, stablecoin, and central bank digital currency. She discussed how banks are engaging in the cryptocurrency ecosystem and reviewed key regulatory developments. Frankly, Brooke's presentation was so informative that even I finally understood the basic elements of cryptocurrency.

Barbara McAneny, MC, CEO, NM Oncology & Hematology Consultants, provided her thoughts on the failure of our attempts to reform our health care "system." Dr. McAneny was the President of the American Medical Association and served on its board for 10 years. She discussed why the Affordable Heather Care Act (Obamacare) missed the mark, why the private practice of medicine may not survive, and what is at stake. She posed the question, "Can we reform our health care system, or is it too late?" And she provided some ideas that, in her mind, could potentially make a huge difference in the state of America's health care system. Needless to say, Dr. McAneny knows health care inside and out and was a huge hit as a speaker.

The theme for the convention was "Top Gun – Feel the Need . . . The Need to Succeed". Thanks to Jay Jenkins, we were lucky enough to have an actual Top Gun pilot as our keynote speaker. What an honor and treat that was! Edward "Stevie" Smith had a 22-year career as a Naval Officer and Strike Fighter Pilot in the U.S. Navy. He served as the Commanding Officer of the Navy Fighting Weapons School, TOPGUN, STRIKE, and Strike Fighter Squadron 34. His staff tours include instructor at the Navy Fighter

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Weapons School, TOPGUN, serving as the Standardization Officer and the Navy's Subject Matter Expert for GPS Weapons. His talk was incredibly fascinating. His stories about combat missions and landing on a carrier at night in turbulent waters makes one wonder how TOPGUN pilots stay alive. Stevie is one cool customer.

As one of the final orders of business, the NMBA acknowledged Jay Jenkins, who stepped in the last several months as acting NMBA President after our friend and colleague Lonnie Talbert relocated during his term. Many thanks to Jay for his continued support of the NMBA.

As a final order of business, the NMBA elected its new officers and board members for 2022-2023. They are as follows:

- **President:** David Hockmuth, Wells Fargo Bank, Albuquerque
- **President-Elect:** Mark Horn, Pinnacle Bank, Gallup
- **Treasurer:** Mike Lowrimore, Bank of the West, Albuquerque

New Board Members

- Kamal Ali, PNC Bank, Albuquerque
- Aaron Emmert, Pioneer Bank, Roswell
- Scott Czarniak, First National 1870, Albuquerque

State Revenue Picture and Possible Legislation

Recently, state economists presented to the Legislative Finance Committee with the state's most recent revenue outlook. As one legislator said, "And the news seemed almost too good to be true." A projected $10.9 billion in revenue for the coming fiscal year sets a new record for New Mexico. It is more than twice the $5.4 billion the state took in just over a decade ago. It represents a projected $2.5 billion in "new" money for the budget year beginning July 2023 (the increase over last year's revenue), a 29% growth from the FY23 recurring budget. So what is the 2023 Legislature likely to consider in the way of new programs and pressing needs of the state? Here are some possibilities:

- Revising the state's tax code. Perhaps lowering the gross receipts taxes and decreasing taxes for middle-class workers.
- Infrastructure investments in roads, bridges, and dams.
- Public education
- Health care
- Expansion of broadband infrastructure
- Safe and efficient water systems
- Trust funds for future state needs ■

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WASHINGTON UPDATE

ROB NICHOLS
PRESIDENT AND CEO
AMERICAN BANKERS ASSOCIATION

The interest in cryptocurrencies and digital assets is undeniable – even in the face of recent volatility in digital asset markets. Americans want them: from the casual dabbler to the serious investor, from Gen Zers to boomers, it seems everyone wants a bite at the crypto apple.

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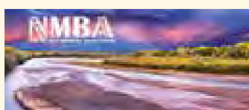

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BREAKING DOWN THE DEBATE OVER DIGITAL ASSETS

As I traveled the country this summer speaking at various state bankers association conventions, I'd always ask this question of my audience: How many of you have clients and customers asking you about cryptocurrencies and digital assets? And nearly everywhere I went, nearly every hand would go up.

The interest in cryptocurrencies and digital assets is undeniable – even in the face of recent volatility in digital asset markets. Americans want them: from the casual dabbler to the serious investor, from Gen Zers to boomers, it seems everyone wants a bite at the crypto apple. Many banks want to engage, too – as digital assets become more popular, and those banks are exploring ways to meet the needs of customers who want their bank to be the custodian of these assets.

I've written previously about the merits of banks being able to take on custodial roles for digital assets – there are many – and the need for a regulatory architecture that will support them in taking on these roles if they choose. That's an area where ABA continues to advocate for banks' ability to enter the digital asset space safely and soundly. But it's just one of the debates currently brewing over crypto.

There are several others of which bankers should be aware:

Who should regulate? One key quandary facing policymakers right now: what's the right way to regulate crypto, and to which agency should that authority be delegated?

Currently, the Securities and Exchange Commission and the Commodity Futures Trading Commission are both vying for the role of crypto cop. Two separate bills have been introduced this summer – one by Sens. Cynthia Lummis (R-Wy.) and Kirsten Gillibrand (D-N.Y.) and another by Sens. Debbie Stabenow (D-Mich.) and John Boozman (R-Ark.) –

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that would delegate most of this authority to the CFTC. Simultaneously, there are some in the crypto community calling for the creation of a whole new regulatory agency dedicated to digital asset supervision, though this seems far less likely.

Regardless of which entity ultimately ends up with regulatory authority, it is imperative that it develops clear definitions of digital asset products that are based on the risk that each category of digital asset carries. Working with the banking agencies, any prospective crypto regulator must also ensure a level playing field between bank and non-bank entities in the digital asset markets and establish clear guidelines for risk management and consumer protection.

Payments system access? Another key question is the extent to which nonbank crypto firms should have access to the payment system. The Federal Reserve took a significant step toward answering this question in mid-August when it finalized a framework for assessing which entities may be granted payment system access. This framework creates a tiered system for evaluating incoming requests, and under it, institutions that engage in novel activities would undergo a more extensive review.

Access to the payments system is a significant privilege with many responsibilities. As the Fed begins evaluating new requests for access, we'll be watching carefully to ensure that these new guidelines appropriately account for the inherent risks that come with some of these new financial players.

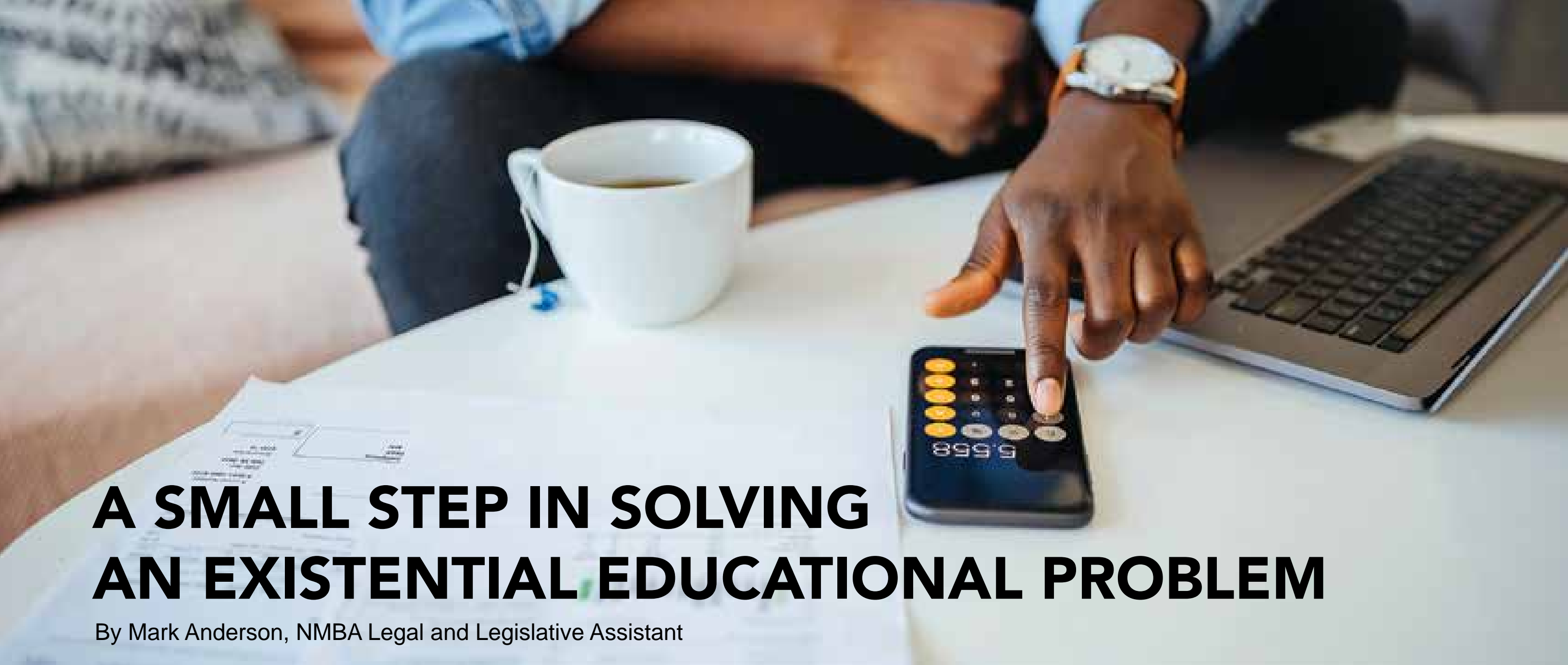
Is there a use case for a CBDC? Finally, there's the question of a central bank digital currency and whether there's a use case for it in the U.S. As ABA told policymakers in several comment letters and testimonies over the last year, our view is that no such case exists – for every problem that proponents say a CBDC could solve, the fact is that there are already solutions available that don't involve a government-created currency. Financial inclusion is just one example: banks are already making great strides to bring more unbanked households into the financial system by offering Bank On-certified accounts.

Not only would a CBDC be duplicative of private-sector solutions that already exist, but it also has the potential to have an incredibly damaging effect on bank balance sheets and the flow of credit to households and businesses if the Federal Reserve were to become a competitor for bank deposits.

These ongoing debates underscore an urgent need for a fair, well-calibrated regulatory framework for digital assets that promote responsible innovation while minimizing systemic risk and protecting consumers. And that's a framework we'll continue to fight for. ■

NMBA Welcomes New Associate Member Upgrade, Inc.

The New Mexico Bankers Association is pleased to welcome a new Associate Member, San Francisco-based digital banking company Upgrade, Inc. Upgrade has facilitated $16 billion in loans with financial partners and a seasoned consumer lending team. Upgrade partners with banks, who purchase their facilitated loans, including personal loans, cards, and auto refi loans, to solve for margin compression, balance sheet diversification, excess liquidity deployment, and fee income replacement. Upgrade's asset purchase program incorporates with existing ALM strategies and is flexible with custom credit criteria, national or geographic, no minimum commitment, 30-day average onboarding, and loan servicing. ■



A SMALL STEP IN SOLVING AN EXISTENTIAL EDUCATIONAL PROBLEM

By Mark Anderson, NMBA Legal and Legislative Assistant

If you follow the machinations of the United States Congress and the Executive Branch with any regularity, you will begin to notice that most of what actually ends up being enacted falls along the lines of corporate tax cuts, subsidies for already absurdly profitable entities, continually expanding military budgets with no end in sight, and other priorities that have no relation to democratic popularity or will. However, in the past couple of months, the Biden administration has addressed the concerns of average Americans in the form of concrete policy, something that is sadly rare in Washington, D.C. Most notably, President Biden announced a student loan debt relief plan that should genuinely help a substantial amount of people. Biden's decision is a relatively simple, effective and helpful policy, and the reactions in various factions have also been informative.

Biden announced he would cancel $10,000 from every student loan balance owned by the federal government (about 80% of the outstanding total), subject to an income cap of $125,000 for individuals and $250,000 for families. In addition, Pell Grant recipients (often a proxy for low-income debtors) are eligible for up to $20,000 of relief. In total, nearly half of all student loan debtors will receive full cancellation, and it is estimated that 90% of relief will go to people earning less than $75,000. The Biden administration has also announced it will begin taking student debtors out of default, which will help them restore access to other credit.

These policy decisions are a good start in solving what has become a massive problem. The student loan debt crisis has had cascading effects in recent years, preventing multitudes of young people from robustly participating in the economy and discouraging students from pursuing higher education. According to a Penn Wharton study of the policy, about 60% of the benefits would accrue to people in the bottom 60% of income. Overall, the relief is largely targeted toward lower-income debt holders, which cuts against the argument that many college graduates from wealthy families will largely benefit from debt relief. The vast majority of students from wealthy families have their college paid for by their parents, which is fine, but these aren't the students incurring massive amounts of debt. The discussion of wealthy students benefitting from student loan debt relief is simply a red herring by people who don't want any relief at all.

This decision from the Biden administration is a small step in what, unfortunately, needs to be a thorough rehabilitation of both America's public education system and, more importantly, how Americans view education on the whole. It's fairly easy to see how the accelerating costs of higher education and the subsequent debt it leaves many students have made more Americans suspicious of its efficacy. When a college education leaves a student with shaky job prospects and a mountain of debt, it's difficult to argue its inherent worth. Therefore, it becomes much easier to cast doubt on the very concept of higher education itself.

In an ideal world, education should be viewed as a noble pursuit by its very nature, but, in America, education has taken on an extraordinarily mutated form, and the most obvious reason is the ballooning costs attached to it. Many parents are under tremendous financial strain while sending their children to college, so students often feel pressure to major in subjects that, in their minds, will lead to greater financial reward.

Higher education in America has turned into a knock-down, drag-out attempt to get out of financial destitution for many students. Any notion of pursuing higher education to simply improve one's intellect, critical thinking skills, and understanding of the world is completely out the window for all but the most fortunate students. In the framework of this country, pursuing higher education to better one's intellect is viewed as a frivolous pursuit undertaken by unserious individuals. This is a byproduct of the financial structure of the college experience in America. When a society starts fully treating education as a commodity rather than a right and a necessity, it doesn't bode well for the future of its population. We are at that point in the United States.

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A recent piece in Slate details the increasing absurdity of higher education in America, highlighting how truly captured it has become by financial demands. As one section of the article states,

> "...many colleges hire expensive consulting firms to help them manage a complex process of marketing, admissions, and pricing. The firms design social media campaigns and produce the flood of glossy brochures that pour through the U.S. postal system every year. They take the wealth of detailed financial information that parents are required to disclose on the Free Application for Federal Student Aid, or FAFSA, and feed it into the same kinds of complex algorithms that airlines use to constantly change the price of seats in the months, weeks, and days before a flight. They also use a probabilistic strategy for deciding whom to admit, based on a combination of how much they think parents are willing to pay and how likely students are to enroll. Because of online systems like the Common App, it's easy for students to apply to many colleges. At less desired colleges – the safety schools and fourth choices – yield rates, meaning the percentage of admitted students who enroll, are often below 20 percent. So they admit 3,000 students to fill a freshman class of 600 and hope that past statistical patterns hold. If too many students enroll, there's no room in the dorms. Too few, and the college goes broke. The whole process is called 'enrollment management.'"

The Slate article further details how a sense of an imagined scarcity of college admissions slots influences students to make rushed decisions, sometimes putting themselves in an even more precarious position financially when it may not have been necessary.

> "Understanding the true nature of the college market should reduce some kinds of student stress. If you're a high school graduate in reasonable academic standing, there are scores of good colleges ready to admit you. The real market tuition price in the big middle of the higher education sector is probably about $25,000, not the $50,000 or $60,000 you might have heard. Applying to college there isn't like being vetted to join an exclusive social club. Nobody is really judging your worthiness for financial aid. College is just another service with a price."

High school students – when attempting to select the right college – are left to weigh a complex web of pros and cons, many of which involve financial decisions. At 17 or 18 years old, it is easy to be guided by an imagined sense of what you should do or what will be financially beneficial years in the future. At such a young age, it is often difficult to balance financial concerns with concerns for personal welfare, which can lead to poor decisions. It's fairly unfathomable that people could be opposed to this debt relief, as it is largely debt held by the federal government. Any argument for a continuation of the status quo is simply an argument for continual economic and educational deterioration simply for the sake of keeping the status quo. The more inaccessible and expensive higher education becomes, the less educated our society will become. Nobody, in good faith, can argue that a less educated society is positive.

Education has been so divorced from its original intent in America that there are actually politicians and members of the media arguing that even Biden's modest student loan debt proposal is way overboard, effectively equating it to a government handout. Most notably, Americans for Prosperity, the organization founded by the billionaire Koch brothers, immediately came out against the move with this statement: *"This shameless handout will only push education costs even higher, cause people to take out even bigger loans, and set a dangerous precedent that the government will just come along and erase their debt in the future."*

Since the announcement of student loan debt cancellation, many powerful interests have claimed that the Biden administration's legal justification is faulty, while the White House has cited the 2003 HEROES Act as the basis for its decision. The almost uniform condemnation of student loan debt relief by powerful interests has been extremely telling and is instructive of a larger trend. Any policy decision that uses the government to ameliorate some of the struggles of average people is met with widespread condemnation by most media, politicians, corporations, and business leaders. The fact that we have so many people in America living in poverty is a conscious policy decision, as is having millions of young people buried under mountains of debt. These aren't laws of nature but conscious decisions made by people in positions of power. Decisions like canceling student loan debt let people know that the federal government actually has the ability to ameliorate, not just immiserate. ■

HOW BANKS CAN RESPOND TO THE SHIFTING FUNDING LANDSCAPE

By Rob Blackwell, Chief Content Officer, IntraFi

With banks still flooded with cash in the wake of the pandemic, many are waiting to raise deposit rates, content to watch some excess liquidity run off the balance sheet. But in a rising rate environment, some analysts are raising questions about whether banks risk waiting too long. Indeed, over the next 12 months, 77% percent of bank executives expect deposit competition to increase, and 90% anticipate higher funding costs, according to IntraFi's most recent quarterly survey.

To better understand how banks should be thinking about funding, we recently sat down with Neil Stanley, founder and CEO of The CorePoint, for Banking with Interest. Neil shared his thoughts on the Federal Reserve interest rate outlook, how soon banks should be responding, alternative investments to consider, and much more.

What follows is our conversation, edited for length and clarity. *(This article was updated on July 19, 2022.)*

How should bankers be responding to the Fed? Should they be raising rates?

Yes, but not across the board. To ignore that rates are rising in the wholesale markets would be a mistake; in the non-loan market, banks can get good rates at a very short duration. Why would they not pay something closer to those rates in this environment, knowing that the Fed is going to be aggressive? It's hard to understand that banks can simply opt out when the wholesale world gives them riskless profit opportunities.

Some banks gained so many deposits during the pandemic that they actually want a certain amount off their books. Are they right?

A bank may have a low loan-to-deposit ratio relative to its history, but it can make money by deploying assets today – that's the part that's hard for some to see. Digital banks and neobanks, competitive threats that didn't exist 15 years ago, are more than happy to relieve banks of the burden of paying something materially less than Fed Funds for insured deposits. So, I think the question [for banks] is, do I have enough capital? If so, I'll take these assets. But I have to figure out how to negotiate with depositors without paying everybody higher rates.

Are bank leaders adequately communicating the value of depositors and deposits today?

No. The conversation within banks during the pandemic was that they would stop looking for deposits and that it would be fine if some left. If things have changed, unfortunately, sometimes an executive team will soften or even revise a posture without [adequately communicating] the change, and the front line continues to operate under the old marching orders. So, the top of the house needs to ask itself if it has communicated those changes to the front line.

You regularly post on LinkedIn. Recently, you wrote about multiple deposit pricing betas simultaneously. What did you mean?

Technically, the deposit beta is a single ratio of the percentage change in total interest expense relative to the change in

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wholesale interest rates. So, there's not really a multiple beta; I'm sort of distorting the concept, but it gets bankers' attention. To optimize results, management teams need to recognize different rate sensitivities for different products and deposit bases. For example, the rate adjustment needed on a common savings product is very different than on a high-yield money market account that's been promoted as high-yield.

The fastest growing segment of deposits from 2018 and 2019 were actually time deposits, which many consider a relic of the past. Bankers knew they didn't want to reprice their whole portfolio of non-maturing deposits, and depositors saw a high enough interest rate to open an account. That combination caused CDs to grow at a 20% annualized rate, and we're going to see that again.

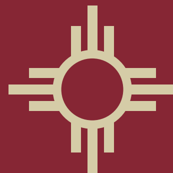
What happens to deposits if the Fed continues raising rates aggressively?
It's going to be an ongoing evolution or adjustment. Prior to the Great Recession, we talked about Fed policy being accommodative or restrictive. The notion of a stimulative policy was outside the boundaries of sound economics. Ultra-low Fed Funds and quantitative easing have brought trillions in fixed income securities onto the government's books. And we went too far. We used performance-enhancing drugs until we overdosed, resulting in a disease called inflation.

But you know, for every interest rate, there's a payer and a receiver. The receiver thinks one thing, and the payer thinks something else. So, the idea that low-interest rates are always good for everyone I don't think holds true.

What are you recommending bankers do now?
Bankers should be continuously assessing their capacity for capital as well as their investment options. Wholesale needs to be part of the mix, not just on the funding side but also on the investing side. Not having a big bond portfolio doesn't make sense when bonds are as profitable as loans. Also, the one-price-fits-all notion [of retail banks] shouldn't be the thinking anymore, especially with the technologies we have today that enable us to customize pricing for depositors.

What's the most common mistake bankers are making?
Pursuing low-cost funds no matter what. It feels good not paying for deposits; it also feels good to think about the yield potential of our assets. But at some level, more money is made with a smaller spread and higher volume.

Is there something I should have asked but didn't?
Maybe, what do I think will surprise bankers in the next few years? I think they're going to experience a refinance wave on the deposit side. Banks that hold time deposits today, if they haven't fortified their early withdrawal penalties, might be surprised when other financial institutions – some traditional, some nontraditional – come after those. ■



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INVERTED YIELD CURVE MAY BRING HEDGING OPPORTUNITY

By Jay Kenney, PCBB

This past spring, the US bond market, where many community banks are invested, flashed a common recession warning: the yield curve briefly inverted, with short-term debt paying more than longer-term loans.

Traditionally, an inverted yield curve has been an early predictor of a coming recession. But the correlation has grown weaker over the past two economic cycles. In the current market, another explanation of the inverted yield curve could be that the yield on two-year debt is rising at a faster pace in response to the Federal Reserve's aggressive tightening of monetary policy. We dive deeper into what really impacts the yield curve and how your bank can take advantage of this unusual circumstance.

Multiple factors shape yield curves

Both short- and long-term considerations determine the shape of the yield curve. In the current environment, a mix of economic and geopolitical events have nudged short-term interest rates up, while slowing down the momentum of increases in long-term rates.

Fed rate hikes are the big factor in this occurrence of an inverted yield curve. In 2020, the Fed cut its overnight rate to near zero as part of an effort to limit the COVID-19 pandemic's effects on the economy. Now, however, the Fed has begun to raise its benchmark rate to counter the effects of runaway inflation. The Federal Reserve's current dot plot (used for signaling the Fed's outlook for the path of interest rates) shows the median year-end projection for the Fed Funds rate moved up to 3.4%. The estimate for the end of 2023 was boosted to near 3.8%.

When the Fed raises rates, other rates typically go up as well. But the increase can sometimes combine with other economic factors to have counteracting effects on different terms along the yield curve. Right now, short-term bond yields are increasing, but longer-term bond yields haven't gone up by much. That's because strong international demand for U.S. Treasury bonds, plus quantitative easing, has made longer-term bonds relatively more expensive – and pushed their yields down.

An inverted yield curve brings opportunities

No one can know for sure when the next economic recession will begin. But financial institutions may be able to take advantage of two potential opportunities that the inverted yield curve offers.

1. **The first opportunity is in buying bonds.** When the yield curve is in its usual upwards-sloping shape, investors earn lower yields for short-term debt and higher yields for longer-term bonds.

   In an environment of rising interest rates, bond buyers have to choose between longer-term debt, which carries a better yield, and shorter-term debt, which yields less but gives a buy-and-hold investor more opportunities to purchase newly issued bonds at higher rates. But when the yield is inverted, bond buyers get the best of both worlds: higher yields and more opportunities to buy new bonds as rates rise.

2. **The second opportunity is a chance to hedge floating-rate debt with an interest-rate swap.** Any time investors use an interest-rate swap hedge, they have to consider whether the value of locking in an interest rate justifies the cost of the swap.

   With an inverted yield curve, however, investors can have the best of both worlds. They can lock in a swap rate less than the rate short-term bonds are paying while also giving themselves longer-term certainty of debt payments with a stabilized interest expense. ■

To continue this discussion or for more information, please contact Jay Kenney, SVP & Southwest Regional Manager for PCBB, at www.pcbb.com or by email at jkenney@pcbb.com.

Dedicated to serving the needs of community banks, PCBB's comprehensive and robust set of solutions includes cash management, international services, lending solutions, and risk management advisory services.

SWOT-ING AT THE CRISSCROSSING CRYPTO CRACKDOWN

By Theo Kelly, Associate General Counsel, Compliance Alliance

INTRODUCTION

In the 14 years since blockchain technology's invention, banks have been left to compete with emerging business models and new stores of value while operating in an uncertain vacuum of regulatory guidance. The resulting whiplash of lightning-fast innovation seemingly incapacitated the U.S. regulators of currencies, commodities, and securities.

With only crisscrossing guidance offered thus far, it may seem impossible to make a risk-based decision on whether and to what extent a bank should adopt blockchain technology, including cryptocurrency and web3. However, using the tried-and-true Strengths, Weaknesses, Opportunities, Threats (SWOT) analysis, banks can establish a baseline with which to evaluate the impact the crisscrossing crypto crackdown will have on their internal and external environment.

First, here is a refresher on the more recent commentary and actions by banking regulators. We know that Basel will be releasing a second consultation later this year with an eye on a "global minimum prudential framework" to address risks associated with crypto assets. Their first consultation offered a risk-weighting methodology.

The U.S. Office of the Comptroller of the Currency (OCC) confirmed in July 2020 that national banks could offer crypto custodial services. However, Acting Comptroller Michael J. Hsu recently publicly remarked that it is time to "reset and recalibrate." The Federal Reserve Board (FRB) hasn't released much guidance other than to say they will be releasing guidance. The FRB did examine the pros and cons of a Central Bank Digital Currency (CBDC) but "does not favor any policy outcome." And the U.S. Treasury has offered a risk assessment of money laundering risks in the crypto asset space. The FDIC joined the OCC and FRB in their "Crypto-Asset Policy Sprint" statement but has offered little else outside of requiring banks to notify the FDIC prior to engaging in crypto-related activities. The CFPB broadened its own enforcement authority in this space last year, formalized in March by Executive Order: FinCEN. And finally, legislation introduced in early June appears ready to assign rulemaking and enforcement authority to the Commodity Futures Trading Commission (CFTC), leaving the Securities Exchange Commission (SEC) any leftover crypto assets classified as securities.

THE BASICS

It can be difficult to understand and analyze the risks associated with crypto assets if you don't have a grasp of some foundational terminology. Unfortunately, there's a lot of so-called "gatekeeping" in the "crypto community," e.g., folks who use overly complicated lingo to seem more tech-savvy than others. So, here are a few layperson examples to help understand the basic terms and concepts.

What is blockchain?

Have you ever worked on a document at the same time as another person or team? You can see others' initials moving about on the page, followed by their edits to the collaborative document. And the revision history is saved so everyone can see who made what changes. This is a great analogy for "distributed ledger technology" (DLT). But the key difference between DLT and blockchain is that no single authority maintains the data (e.g., OneDrive, Google, AWS). With blockchain, there is no centralized authority holding the data, and the data is not valid unless "approved" by a program that runs on many different devices around the world.

What is a crypto asset?

Crypto assets are much like your everyday tangible assets: cash, contracts, artwork, investments, information, etc.

However, crypto assets are entirely digital. Here, everyone knows your unique address (known as a wallet address) owns those assets because of the transaction information stored on the blockchain. A dollar bill may be compared to a Bitcoin. A contract may be compared to a "Smart Contract." A non-fungible token may be compared to your house deed. Nearly every transaction made in your everyday life can be hosted on a blockchain.

What makes a crypto asset a security versus a commodity versus fiat currency?

A “security” represents an investment in a common enterprise with the expectation of profit solely on the efforts of others (“solely” is removed in actual practice). A crypto asset offered to raise capital for a startup would likely be classified as a “security.”

Crypto assets generally fall into the classification of a commodity. A commodity is a resource nearly identical in all its instances and has a commonly known value, such as wheat. Financial commodities include identical (or nearly identical) futures and options contracts that have commonly known values.

For the purposes of classifying crypto assets, “fiat” is defined as the “lawful money” of the United States. In other words, a currency that represents the debts of the government. You can’t pay your taxes in wheat, for example, but you can use U.S. dollars. A Central Bank Digital Currency (CBDC) would be classified as fiat currency.

THE SWOT

A SWOT analysis considers your internal strengths and weaknesses and external opportunities and threats. This template offers baseline considerations to review the risks and opportunities associated with the emerging crypto regulatory scheme.

Strengths and Weaknesses

- **Management:** The Board and senior managers of the bank have a clear understanding of the existing regulatory parameters surrounding crypto assets, are knowledgeable about the application of those rules to bank offerings, maintain an awareness of emerging changes, and have a system in place to update the bank's operations quickly and efficiently to comply.
- **Internal Controls:** The bank's internal controls are built-out and appropriately monitored and tested to manage the increased credit, liquidity, and transaction risks associated with crypto asset custody, transactions, loans, issuance, and holdings. The bank stress tests contagion risks and enhances areas of identified deficiencies. Where applicable, the bank has consistent margin call triggers, procedures, and communication channels. Evaluations of crypto assets as collateral are reviewed for fair lending purposes.
- **Personnel:** Bank personnel are properly trained to understand and communicate the products and services offered to customers, are aware of and can appropriately mitigate the related risks, the number of assigned personnel is appropriate for the associated risks, and enough redundancy is built into roles to prevent any system failures that may result from the termination of key personnel. Vendors undergo a risk-based due diligence review before business begins and periodically thereafter.
- **Technology:** The hardware and software used to transact, secure, and maintain crypto assets are well-maintained and secure. External auditors are used to test and verify. The bank has a consistent and safe procedure for securing crypto collateral.
- **Insurance:** The bank maintains appropriate levels of insurance related to all facets of crypto asset products and services.
- **Products:** The bank can market and advertise crypto asset products and services in a manner consistent with existing laws and regulations and an eye for fair lending and UDAAP risks. It has reviewed existing non-crypto products and services, identified the potential impacts, and updated those growth strategies to account for the internally driven competition.

Opportunities & Threats

- **Management:** The Board and senior managers of the bank can readily identify risks and opportunities presented by the lack of crypto asset laws and regulations.
- **Personnel:** Personnel are excited to join a bank that offers roles in the crypto asset space; however, this area may also come with increased competition for bank personnel who maintain desirable skills in a new field.
- **Technology:** Rapid advances in technology offer opportunities to quickly adopt and roll out new product offerings and services; however, the maintenance and security of aging software and hardware suffer, and investments in new technology depreciate quickly.
- **Competition:** The bank is an early adopter of crypto products and services but may now lack the resources to act upon new trends, technology, and opportunities.
- **Reputation:** The bank is well-posed to trigger crisis management plans, maintains open channels of communication with relevant stakeholders, and has identified and mitigated risks associated with crypto asset environmental risk factors.
- **Legal and Compliance:** The bank's compliance management system and risk management program appropriately identify and control crypto-asset risks, including the emerging regulatory scheme and the potential for increased litigation.

CONCLUSION

Given what little we know about the future legal and regulatory landscape of cryptocurrency, a comprehensive and bank-specific SWOT analysis may offer some comfort in the uncertainty. Take some time to discuss your bank’s crypto posture with your internal and external stakeholders and analyze the relevant strengths, weaknesses, opportunities, and threats for your bank. Continue getting involved in the discussions surrounding the proposed laws and regulations. And take this opportunity to enhance your risk management program and Compliance Management System to monitor and respond to the crypto regulatory crackdown we all know is coming. ■

BHG BANK NETWORK MEMBERS EARN COMBINED $1 BILLION IN INTEREST INCOME

By Kathleen Connellan, VP, Institutional Relations, BHG Financial

BHG Financial is the leader in unsecured business and personal loans and the creator of one of the country's largest community bank loan and product networks – the BHG Bank Network. Growing to over 1,450 members who purchase these top-performing loans, BHG Financial now reports a record milestone, with its network banks reaching a combined $1 billion in interest income since 2001.

According to a survey from the financial technology firm Jack Henry[1], 67% of community bank executives listed growing loans as their top strategic priority. As a reliable source of interest income, BHG continuously raises the bar on several industry standards, as noted below:

- Year over year through Q2, average daily sales volume on the BHG Loan Hub rose 24%
- Bank members joining the BHG Bank Network increased 41% in the fiscal year 2021 versus the year prior
- Since the start of COVID in March 2020, 21% of U.S. banks[2] have added a BHG loan to their balance sheet
- For the fifth consecutive year, banks from every year of BHG's existence (2001 to 2022) have returned to buy a BHG loan again

"We're proud to stand with our BHG Bank Network members today and for over the past 20 years. As trusted partners during multiple credit cycles, this milestone is a testament to the relationships we've built and continue to build over time," said Al Crawford, Co-Founder, Chairman, and CEO of BHG Financial.

Allowing the banks to supplement in-house originations, BHG Bank Network members have exclusive access to purchase BHG's loans via a secure, online, state-of-the-art loan delivery platform called the BHG Loan Hub. Here, community banks can quickly grow assets and diversify their loan portfolios with top-credit-quality loans through some of the highest-quality borrowers in the nation.

Offering a seamless experience that allows members to locate, review, and purchase loans with complete credit files, banks can choose from millions of dollars worth of available loans for purchase daily. With credit quality remaining consistently stable and asset volume increasing by 70% annually, there's no wonder why the BHG Bank Network continues to expand year after year. "We are always using our members' feedback to improve their experience on the BHG Loan Hub," said Meghan Crawford, President of Bank Division at BHG Financial. "Strengthening a bank's portfolio and bottom line is our top priority; it's also why BHG Bank Network members keep coming back."

As the BHG Bank Network has evolved, so have the offerings to its members. It encompasses multiple fee income opportunities, digital lending and risk management services, point-of-sale financing, and collections – with more on the horizon. BHG introduces these new products and services at their quarterly seminars, bringing banks together for a chance to learn more about their latest innovations.

If you are interested in learning how to become a BHG Bank Network member, please visit BHGLoanHub.com. ■

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[1] *https://ir.jackhenry.com/news-releases/news-release-details/jack-henry-survey-finds-community-and-regional-financial*
[2] *https://banks.data.fdic.gov/bankfind-suite/bankfind*

BHG Financial is transforming the financial industry, leveraging the power of data, analytics, and cutting-edge technology to become one of the best sources for high-performing loans and the creator of one of the largest community bank loan and product networks in the country. Since 2001, BHG has originated more than $12 billion in loan solutions for top-quality borrowers, which community and midsize banks can access via a state-of-the-art loan delivery platform.

BHG Financials' dedication to providing services that meet the needs of its clients has led to the creation of a full family of brands that range from business, consumer, and SBA 7(a) loans to credit cards, collection services, risk management services, and point-of-sale financing.

With record growth year after year, BHG continues to be recognized regionally and nationally, earning a spot on the Inc. 5000 for 15 years running and receiving accolades from Great Place to Work® and Fortune magazine, among others. BHG Financial is partially owned by Pinnacle Bank (PNFP) and has headquarters in Davie, FL and Syracuse, NY. To represent the company's growth and dedication to continuously expanding its services, Bankers Healthcare Group became BHG Financial in 2021. Find out more about the company at https://bhgfinancial.com.

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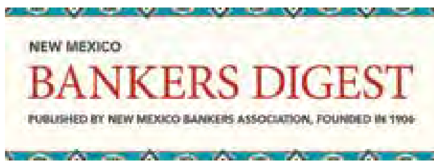

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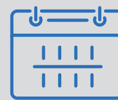

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