# THE *DREADED* ALCO MEETING

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# ABOUT THE AUTHOR

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## DARLING CONSULTING GROUP

Darling Consulting Group is an independent partner to more than 650 institutions helping them to realize the full potential of their ALCO process and financial performance by fostering focused, forward-looking risk assessments along with the development of customized retail and wholesale strategies designed to enhance earnings and manage risks. The objective is to turn ALCO into a profit center.

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I recently had a first-time ALCO meeting with a new client. The meeting was scheduled for 90 minutes, which gave us enough time to establish appropriate perspective and focus, assess the risk position, identify key issues, and discuss tailored strategies that fit their profile. Frankly, 90 minutes was cutting it close, especially for a first-time meeting.

The day before the meeting, the CFO requested we trim it down to just 45 minutes.

“Generally, our ALCO meetings go 30 minutes,” the CFO said. “I don’t think we can keep the team interested much longer than that.”

My response was that their team had invested a lot of resources to implement important change into their ALCO process and get to this first meeting – and that the return on investment could not be fully monetized in just 45 minutes.

“Let’s try to stick to the 90 minutes and see how it goes,” I responded.

The meeting went three hours. Not due to an abundance of content. The dialogue and strategy discussion – led by the CFO – made the three hours feel like 30 minutes.
The next day we received an update from management on decisions made at the meeting and action items (e.g. cash redeployment plan, loan pricing and portfolio decisions, and immediate deposit pricing initiatives), along with the date for next quarter’s ALCO meeting – this time two hours set aside.

It then dawned on me. Most ALCO meetings can get bogged down by economic updates and backward-looking budgetary and other analyses that often result in expedited meetings, which seemingly race to the finish to preempt ALCO members dozing off. The impact? Squandered time and analysis and, most importantly, little if any integrated dialogue among key executives that drives valuable balance sheet strategy discussion.

The pandemic isn’t helping. Many of us aren’t meeting in boardrooms today. Virtual meetings can inhibit that in-person, dynamic collaboration. I recently heard from a banker that they put a moratorium on ALCO meetings.

I understand there are pressing issues –operational challenges, loan forbearances, and PPP activities to name a few. We are all doing more with less these days. However, ALCO cannot be sacrificed. Historical low rates are projecting grave margin pressure for next year. Credit uncertainty has an impact in every balance sheet decision. The deposit surge creates uncertainty in liquidity levels, capital ratios, and IRR profiles. The argument can be made that more time, not less, should be spent at ALCO today.

So how do we transform a stale and dreaded ALCO meeting to one that executives and board members look forward to attending?

We need to flip the script. Reposition your ALCO presentation to target 80-90% strategic focus and 10-20% position analysis. Here are four steps to get started:

## START WITH THE KEY ISSUES

What are the three to four key issues weighing on your institution’s risk position today, and thus should prioritize our conversation and strategy discussion? Tell a story. Open with critical decisions that you will cover throughout the meeting and how they influence strategy. For example, an opening I had for a recent ALCO meeting started with these key issues:

- Cash has mushroomed, and the potential is real that excess liquidity could increase as PPP loans are forgiven. How much is “excess,” for how long, and what factors might alter your assessment? What are our alternatives, and what should our strategy be for excess cash, and why?

- Examine Q2 deposit surge and discuss how it has impacted the current interest rate risk, liquidity, and capital ratio profiles…how does this impact strategy considerations?
- Quantify the timing and dynamics of the NII pressure that is highly likely to materialize over the next two years…what deposit, lending, and investment decisions would be “required” to fill the “gap” and are they tenable?

Setting the stage and tying each of the issues identified into the review of the current ALCO position holds the ALCO accountable for leaving the meeting with executable strategies.

## INITIATE DISCUSSION

Our client meetings don’t go over an hour because we have a 50+ page slide deck. It’s because the focus of the meeting is to initiate discussion with all stakeholders. The best ALCO meetings are when everyone in the room is sharing ideas.

We need to hear the lenders’ front-line experience on deals, competition, and pricing. This will drive a discussion on credit spreads, capacity to extend assets, potential utilization of derivatives to support activity, etc.

We need to hear from the deposit team on expectations and product positioning. This will drive discussion on pricing for liquidity, funding planning, wholesale strategy, etc.

## CONDENSE THE DECK

ALCO reports have gotten out of hand. How do we navigate through a 100+ page report and still leave the meeting with strategic action items? Focus on trimming down the ALCO presentation deck by a third for the actual meeting. This is an art form. Dedicate half the slides to the actual risk position and the other half on thought-provoking strategy items.

Bring creativity to the meeting. I try to envision every slide as a story. What are we trying to tell here? Mix up the content and flow to keep people interested. Presentation matters, both in terms of how risk is depicted in “pictures” and how it is explained/conveyed. Accelerating the clear understanding of risk, and what has changed from the last review and why, frees up valuable time for focusing on the things that matter… executable strategies.

## ANSWER THE QUESTION “WHAT HAPPENS IF…?”

One of the most effective ways to execute a strategy is to run it through the model as a pro forma simulation. The power of graphs to illustrate the impact of a specific strategy idea can help everyone quantify and visualize the results – which gets us closer to execution.

For example, a controversial topic for one of my clients was whether they should be holding mortgage production (vs. selling). One of the chief concerns from the finance team was the impact to interest rate risk in this low rate environment. We assisted by running a simulation to show the impact of holding fixed originations over the next six months – funded primarily with excess cash. The results were surprising to the team. They showed ample capacity to hold production given the strength of the core funding position to support the near-term growth.

## CONCLUDING COMMENTS

I am a “less is more” type of person. But ALCO is where the big decisions are made. An ALCO meeting that goes over an hour is generally a sign that collaboration, idea sharing, and forward thinking has taken place. We need that today more than ever – particularly in a time when whiteboarding and idea sharing are more difficult to come by given how remote business leaders are.

The above ideas are a start. Like I said, this is an art form. It needs to be worked on every quarter. We have clients who have been with us for over 25 years and their ALCO meetings are standing room only. This can be done – and the return on investment will be well worth the time spent in ALCO. Make your ALCO a profit center.

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