News, Analysis and Perspective
for Community Banks by
the Nation's **First** Bankers' Bank

UBB First for Your Success™

Independent

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This Issue:

Invert to improve your chances for Investment Portfolio Performance success.

By UBB Investments

After a late-year rally allowed the bond market to avoid an unprecedented third consecutive year of negative total returns, portfolio managers are left reeling and traumatized by the volatility. Recency bias makes portfolio management even more difficult right now.

After an unexpected Fed pivot in December, investors are asking, "Why now?" and "Where to go from here?" Since 1977, the Fed has had a dual mandate of maximum employment and stable prices. Is their job done? The short answer is yes. The maximum employment piece has not been in doubt, but the pace of private-sector job creation has slowed dramatically. The Stable Prices side of the mandate has proven to be more stubborn for the Fed. However, even with their preferred inflation gauge, Core PCE (Personal Consumption Expenditures Index excluding Food & Energy), running above the FOMC target (3.2% Dec.), the 6-month annualized trend is down to 2%, which is at their target established in 2012.

As a result, the Fed may cut rates this year because they can and not because they have to. The current Fed Funds rate is 200 basis points above the YOY and 325 basis points above the 6-month annualized Core PCE rate. This level is clearly restrictive. If and as the "real" policy rate rises this year as inflation continues to fall, the FOMC will have the luxury of adjusting rates lower to ensure the "correct" level of

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Dwight Larsen A note from the President

At UBB, we start the new year with renewed optimism that 2024 will bring some relief for community banks throughout the industry. In 2023, the banking industry faced its fair share of challenges, from a higher interest rate environment, underwater bond portfolios, and lower levels of liquidity to increased deposit acquisition costs and a couple of large bank failures that briefly shook the banking public's confidence. The list goes on, but the important thing is that community banks held steady and preserved in the face of adversity without skipping a beat. Throughout it all, as we have for the past 49 years, UBB was there by your side, and regardless of good times or bad, we'll always be in the corner of community banks.

This issue's cover story comes from Ben Eskierka, Chief Investment Officer, and discusses how using the skill of inversion can help your investment portfolio during uncertainty.

Jeff Thompson, UBB's Compliance Services Managing Consultant, explores immigration status when making lending decisions.

UBB's partner, ICI Consulting Services, works with community banks to negotiate core vendor contracts for better terms and pricing. In this issue's Q&A, ICI explains when a community bank should start reviewing core contract renewal options and why it is important to start earlier than you might think.

Jason Pruitt joined UBB this past November as a Vice President and Correspondent Banking Officer covering Alabama, Tennessee, and parts of Georgia. Learn more about Jason in this issue's employee spotlight on page 4, then flip over to page 6 to find out how First National Bank of Frederick in Frederick, SD, is *Keeping the Community in Community Banking*.

A new year represents new opportunities, and you can have confidence in knowing that UBB will be working as hard as ever this year to continue providing the products, services, resources and support your community bank needs to compete and succeed. As the nation's First Bankers' Bank, UBB will always be *First for Your Success*.

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restriction with or without a recession or soft landing. The focus should be on what the Fed will do rather than what the Fed should do. The reward will only come for those who get the first one right.

The long-term question for investors is, where is the natural rate or r*(r-star)? The Fed Funds rate neither stimulates nor slows down economic activity. The Fed says it's 2.50% long-term (based on Dec. SEP), but the market says it is more like 3.25%. Either way, the Fed could cut and still be well above the presumed neutral rate. Since the last hike was in July and historically, the average time from the previous hike to the first cut has been six months, it is less if, but when, the Fed will cut and by how much.

My wife has a guilty pleasure in the wintertime, which is her electric blanket. Her blanket is warm, cozy, and not easy to come out from underneath. This example is a lot like the current Fed Funds rate. It, too, is warm and rewarding, but deep down, we know we should shed the blanket and get up and move around. Too much of a good thing can set us up for failure down the road.

It isn't easy to make predictions, especially about the future. Still, with yields at fifteen-year highs and the yield curve noninverting (which it always does before a recession) after being inverted for a near-record 80 weeks, it is an excellent time to consider a new strategy.

To help us, we turn to Warren Buffet's business partner and right-hand man, the late great legendary investor Charlie Munger, who famously said, "Invert, always invert." Turn a situation or problem upside down. He knew that it is in the nature of things that many challenging problems are best solved when they are addressed backward.

What happens if all of our plans go wrong? Where don't we want to go, and how do we get there?

Inversion ranks as one of our most versatile and adaptable skills because it can be applied to almost anything.

For example, rather than focusing on achieving success, *Inversion* encourages you to consider how to avoid failure. It is more a case of finding the least harmful way to play the coming easing cycle.

What failures do you want to avoid?

1. Investing in products that are not easily understood.
   - Know your limitations and understand your competency. Try to avoid acting outside of it.

2. Extending an already extended duration.
   - After all of the hand-wringing and angst over negative AOCI, you can shorten the duration and increase yield.

3. Staying too long in the comfort of cash (electric blanket).
   - The reinvestment risk and the immediate repricing may be a trap that is avoidable.

Please connect with your UBB Investment Representative to help you brainstorm on inverting your thinking for investment portfolio success. Don't forget to register for the 2024 ALMEdge user conference on Friday, April 5th at www.ubb.com/events.

When should my community bank start reviewing our core contract renewal options?”

By ICI Consulting, Inc

Based on our experience, the best time to begin a core processing evaluation project is 30-36 months before your current core processing agreement expires.

1. Starting an evaluation at this point sends a message to your current vendor and potential vendors that your bank is serious about the project, and it creates an environment for aggressive competition; your bank will receive the **best financial results when there is aggressive competition.**

2. Since the beginning of the pandemic, core vendors have experienced **staffing and delivery issues**. As a result, the vendors’ responses to RFPs, availability for presentations, and project implementations have caused delays and the need for time extensions.

3. Banks need sufficient time to evaluate and vet competitive alternatives thoroughly. **On average, banks should expect core evaluations to last 12 months**; the projects may extend longer if they are complex.

4. If the bank decides to convert to a different core system, the conversion lead time varies by core vendor. We see the typical desired **vendor lead times between 15 and 24 months to go live** on the new system. (Refer to #2.)

5. If the bank decides to renew with the current vendor, the new, **improved pricing and business terms will become effective immediately**. This will result in significant savings before the end of the current agreement. The last years of a core processing term are the most expensive for the bank; therefore, avoiding those years with updated pricing is a windfall of savings for the bank.

To request more information about how ICI can help with your Core Contract Renewal, visit www.ubbrequest.com.

Announcements

UBB Welcomes

Darci Forkapa, Vice President, Correspondent Banking Officer, joined UBB’s sales team in February. She will be developing and strengthening relationships with community bankers in Michigan and Ohio. Darci joins UBB with over 20 years of B2B commerce experience in cybersecurity, software and banking solutions.

United Bankers' Bank
Call Report (unaudited)
12/31/2023

Balance Sheet (000's)

Assets:

Cash and Due from Banks	$ 167,611
Investments	$ 163,359
Fed Funds Sold & Securities Purchased Under Agreement to Resell	$ 55,249
Loans	
Outstanding	$ 750,004
Loss Reserve	$ (12,485)
Other Assets	$ 42,782
TOTAL ASSETS	$1,166,520

Liabilities and Capital:

Deposits	$ 675,878
Fed Funds Purchased	$ 226,737
Other Liabilities	$ 139,303
Equity Capital	$ 124,602
TOTAL LIABILITIES & CAPITAL	$1,166,520

INCOME STATEMENT (YTD)

Interest Income	$ 49,176
Interest Expense	$ 29,431
Net Interest Income	$ 19,745
Loss Provision	$ 132
Net Interest Income (After Provision)	$ 19,613
Other Income	$ 18,168
Total Income	$ 37,781
Operating Expenses	$ 32,522
Securities Gains (Losses)	$ (1,239)
Net Income Before Taxes	$ 4,020
Tax	$ 758
NET INCOME	$ 3,262

Employee Spotlight

Jason Pruitt

Vice President, Correspondent Banking Officer
678-972-3515 • jason.pruitt@ubb.com

Family Members: Ashley (wife), Camden (25), Caitlin (23), Elijah (19), Jordan (19) and Jackson (17).

Pets: Dexter, our Shi-poo.

What do you listen to on your drive to work: Classic Rock.

Interests: Traveling with my wife, watching college sports.

If I could live anywhere in the world, I would live in: Ketchikan, Alaska.

If I could have one super power (besides flying), it would be: Teleportation.

Many people don't know that: I am a "retired" college sports official.

If I was not working in banking, I would: be in Law enforcement.

I started working at UBB on: November 3, 2023.

My favorite part of working for UBB: The people and culture at UBB.

The best advice I ever got was: Treat others the way you want to be treated.

First For Your Success means: We are the first Bankers Bank, will never compete for business with community banks and will always be an ally with the community banking industry.

Jason and Ashley with Camden, Caitlin, Elijah, Jackson and Jordan.

Jason and Ashley in Ketchikan, Alaska this past July.

Jason fishing in Alaska.

Immigration Status and Its Relevance to Lending Decisions

By Jeff Thompson, CRCM

Not long ago, we had a question from a banker with a credit applicant whose immigration status was unclear, and the banker was concerned about denying a loan request because of that status. The concern stemmed from the bank's inability to know whether the applicant would remain in the U.S. or leave the country, voluntarily or involuntarily, before the contemplated loan was satisfied.

When we answered that question, our chief source was Regulation B (the Equal Credit Opportunity Act) and its official staff commentary. At 12 CFR 1002.6(b)(7), the regulation reads, "A creditor may consider the applicant's immigration status or status as a permanent resident of the United States, and any additional information that may be necessary to ascertain the creditor's rights and remedies regarding repayment." The interpretive ruling further supports this statement. "1. **National origin - immigration status.** The applicant's immigration status and ties to the community (such as employment and continued residence in the area) could have a bearing on a creditor's ability to obtain repayment. Accordingly, the creditor may consider immigration status and differentiate, for example, between a noncitizen who is a long-time resident with permanent resident status and a noncitizen who is temporarily in this country on a student visa." The interpretive ruling takes it a step even further. "2. **National origin - citizenship.** A denial of credit on the ground that an applicant is not a United States citizen is not per se discrimination based on national origin."

In the case of the bank that reached out to our hotline, the applicant in question presented a temporary driver's license, proof that he was a non-resident alien, and a temporary work visa that would expire in 2025. The borrower was seeking a long-term loan to finance the purchase of an automobile. The applicant's temporary residency and short-term work visa caused the bank to ask us about the applicant's immigration status. When the question was initially asked, the answer was pretty straightforward.

Then…
On October 12, 2023, the CFPB (Bureau) and the Department of Justice (DOJ) issued a joint statement "cautioning that financial institutions may not use immigration status to discriminate against credit applicants illegally." That statement is redundant, as banks cannot illegally discriminate against credit applicants for any reason. This guidance does not necessarily conflict with Regulation B and is consistent with blogs the Bureau published on this subject in 2022 and 2023. However, in both blog posts, the concerns were more systemic than a single loan application.

The Bureau and the DOJ issued their warning to ensure banks do not arbitrarily utilize Section 6 of Regulation B to deny otherwise qualified applicants from obtaining financing to start their lives in the U.S.

Not mentioned in the blog posts or the latest joint statement are the rules banks must follow when a new customer applies for a deposit account, loan account, or other bank service.

The USA PATRIOT Act requires banks to have solid Customer Information Programs (CIP) for all new customers, and other AML/CFT rules require Customer Due Diligence and Enhanced Due Diligence where appropriate. In addition, neither the Bureau nor the DOJ have any mandate that speaks to the safety and soundness of the Bank.

Many of the counterpoints above were also included in a November 1, 2023, letter from eleven Republican Senators who serve on the Senate Banking Committee to CFPB Director Chopra and Attorney General Garland. The Senators criticized the agencies for not subjecting this departure from years of Regulation B interpretive rulings to a formal rulemaking process. The Senators concluded their letter by asserting the joint statement "poses serious risks to financial stability" and called on the agencies to retract the statement and "instead endorse risk-based lending practices that promote safety and soundness in the banking sector." Whether or not the Director and A.G. give the letter any credence remains to be seen.

In summary, banks should ensure policies or practices do not provide for any kind of illegal discrimination against immigrants and that individual loan applications are considered appropriately. Immigration status should only affect a bank's evaluation of repayment risk and should be documented thoroughly. We also recommend discussing this topic with your primary Federal regulator the next time you have the opportunity so you can understand their stance on this sensitive topic.

If you need any support or assistance regarding this or any other regulatory compliance matter, check out our website at www.ubb.com/consulting-services/compliance-services.

Jeff Thompson, Vice President, Managing Consultant - Compliance • 614-369-0054 • jeff.thompson@ubb.com

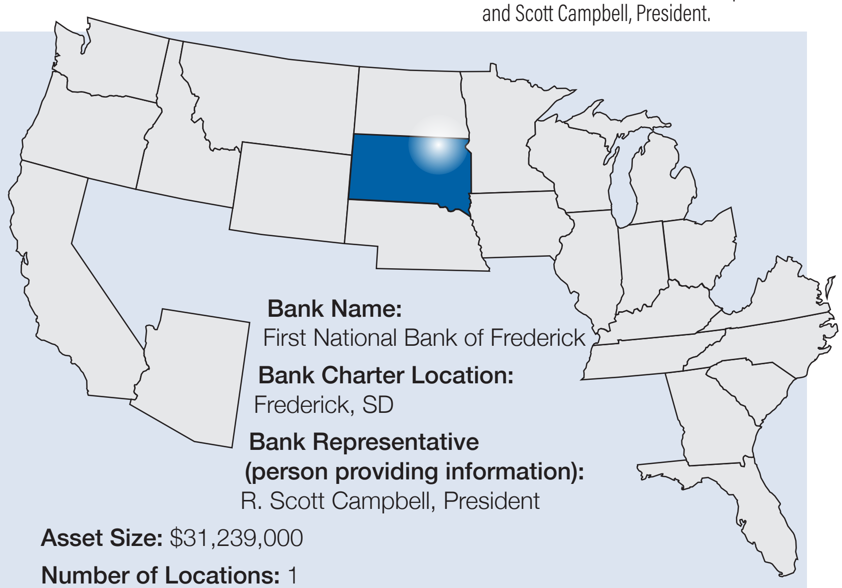
Keeping the *Community* in Community Banking

First National Bank of Frederick • Frederick, SD

On the banks of the Maple River, just 7 miles south of the North Dakota border, lies the town of Frederick, SD. For almost as long as Frederick has been a town, First National Bank of Frederick has been the heart of the community. First National Bank of Frederick is a 5th generation bank that prides itself on providing quality hometown service. We contacted bank President, Scott Campbell, to learn how First National Bank of Frederick is *Keeping the Community in Community Banking*.

First National Bank of Frederick - Frederick, SD

Four person team of First National Bank Frederick Kelli Millard, Jennifer Morlock, Teresa Campbell, and Scott Campbell, President.



Bank Name:
First National Bank of Frederick

Bank Charter Location:
Frederick, SD

Bank Representative (person providing information):
R. Scott Campbell, President

Asset Size: $31,239,000

Number of Locations: 1

Number of Employees: 4

Year Bank was Incorporated: 1882

City Population: 225

What is your community most known for?
Many Finnish immigrants homesteaded in the Frederick Area. Don Larson, a New York Yankee pitcher, hunted pheasants in the Frederick area after he pitched his perfect game during game 5 of the 1956 World Series.

How is your bank involved in the community?
As a small community bank in a small community, our bank is involved in almost every organization in the community. Our employees serve as firefighters, EMTs, church parish board members, town council members, town finance officers, fire district board members, development corporation members, and North Brown Community Foundation board members and are active in local civic groups.

Do you have any goals or programs to encourage bank employees to be active in the community?
We don't have any programs. Our employees understand the importance of being involved in the community.

What makes community involvement important to you and your bank?
Through community involvement, we help our small community navigate through the challenges that small towns face. A community bank will not survive if it doesn't get involved in the community in which it serves.

What do you like best about your community?
Living in a community where you literally know everybody provides a safe and stable environment to live. When we have a community member that is struggling, the community comes together to help those people in need. Frederick is a wonderful place to raise a family. We have an excellent K-12 school that provides a quality education for our children. Our area offers fantastic outdoor activities for people to enjoy, such as hunting, fishing, water sports, winter sports, and just enjoying the beautiful scenery on the prairie. Frederick is also a short half-hour drive from Aberdeen, which has 30,000 people, and around three hours from Sioux Falls, SD, and Fargo, ND.

What do you like best about being a community banker?
The personal relationships you build with each customer - We know all our customers by name. Our customers are our neighbors and friends with whom we have been doing business for generations. We view our customers like family rather than just a customer with a number. It is reassuring for our customers to know they always have a familiar face to meet them when they enter our bank. People don't get that in a large bank.