



# Bank Management

By Timothy W. Koch, S. Scott MacDonald

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### **Review**

1. Banking and the Financial Services Industry. Credit Crisis of 2007-2009. Impact on Banks and the Banking Environment. How Do Banks Differ? Trends in the Structure of U.S. Banks. Organizational Structure and Financial Services Business Models. S-Corporation Banks. Financial Services Business Models. Transactions Banking versus Relationship Business Models. Universal Banking. Different Channels for Delivering Banking Services. Branch Banking. Automated Teller Machines. Internet (Online) Banking. Call Centers. Mobile Banking. 2. Government Policies and Regulation. Historical Bank Regulation. Products and Services. Goals and Functions of Depository Institution Regulation. Ensure Safety and Soundness and Provide an Efficient and Competitive System. Supervision and Examination. New Charters. Federal Deposit Insurance. Product Restrictions: Depository Institutions versus Nondepository Institutions. Shortcomings of Restrictive Bank Regulation. Maintaining Monetary Stability and the Integrity of the Payments System. The Role of the Central Bank in the Economy: The Federal Reserve System. Monetary Policy. The Federal Reserve's Crisis Management Tools. The Role of Depository Institutions in the Economy. Efficient and Competitive Financial System. Consumer Protection. Trends in Federal Legislation and Regulation. Key Federal Legislation: 1970-1993. Key Federal Legislation: 1994-2000. Key Federal Legislation: 2001-2006. Key Federal Legislation: 2007-2008. Current Unresolved Regulatory Issues. Capital Adequacy. Regulatory Reform. 3. Analyzing Bank Performance. Commercial Bank Financial Statements. The Balance Sheet. The Income Statement. The Relationship Between the Balance Sheet and Income Statement. The Return on Equity Model. Profitability Analysis. Expense Ratio and Asset Utilization. Managing Risk and Returns. Credit Risk. Liquidity Risk. Market Risk. Operational Risk. Legal and Reputation Risk. Capital or Solvency Risk. Off-Balance Sheet Risk. Evaluating Bank Performance: An Application. Profitability Analysis for PNC in 2007. Risk Analysis for PNC in 2007. PNC's Profitability versus Risk: 2003-2007. Maximizing the Market Value of Bank Equity. Camels Ratings. Performance Characteristics of Banks by Size. Financial Statement Manipulation. Off-Balance Sheet Activities. 4. Managing Noninterest Income and Noninterest Expense. Noninterest Income. Deposit Service Fees. Noninterest Expense. Key Ratios. Which Lines of Business and Customers are Profitable? Line-Of-Business Profitability Analysis. Customer Profitability Analysis. Aggregate Profitability Results from Customer Profitability Analysis. What is the Appropriate Business Mix? Strategies for Managing Noninterest Expense. Cost Management Strategies. Revenue Enhancement. Contribution Growth. 5. The Performance of Nontraditional Banking Companies. The Financial Performance of Goldman Sachs. Goldman Sachs's Income Statement. Goldman Sachs's Balance Sheet. Key Performance Ratios. Risks Faced by Goldman Sachs. Goldman's Risk Profile. The Financial Performance of Mutual of Omaha Bank. Mutual of Omaha Bank's Risk Profile. The Financial Performance of BMW Financial Services and BMW Bank of North America. BMW Bank's Risk Profile. 6. Pricing Fixed-Income Securities. The Mathematics of Interest Rates. Future Value and Present Value: Single Payment. Future Value and Present Value: Multiple Payments. The Relationship Between Interest Rates and Option-Free Bond Prices. The Size of Coupon Influences Bond Price Sensitivity. Duration and Price Volatility. Duration as an Elasticity Measure. Measuring Duration. Duration of a Zero Coupon Bond. Comparative Price Sensitivity. Recent Innovations in the Valuation of Fixed-Income Securities and Total Return Analysis. Total Return Analysis. Valuing Bonds as a Package of Cash Flows. Money Market Yields. Interest-Bearing Loans with Maturities of One Year or Less. 360-Day versus 365-Day Yields. Discount Yields. Yields on Single-Payment, Interest-Bearing Securities. 7. Managing Interest Rate Risk: GAP and Earnings Sensitivity. Measuring Interest Rate Risk with GAP. Traditional Static GAP Analysis. What Determines Rate Sensitivity? Factors Affecting Net Interest Income. Rate, Volume, and Mix Analysis. Rate Sensitivity Reports. Strengths and Weaknesses of Static GAP Analysis. Earnings Sensitivity Analysis. Exercise of Embedded Options in Assets and Liabilities. Different Interest Rates Change by Different Amounts at

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Foreign Exchange Rates and Interest Rates. Price Risk with Foreign Currency.

### About the Author

Timothy W. Koch serves as Professor of Finance at the University of South Carolina. He received his B.A. degree in mathematics from Wartburg College and Ph.D. in economics from Purdue University. He taught at Baylor University and Texas Tech University before joining the University of South Carolina. In addition to his college teaching role, Dr. Koch serves as President of the Graduate School of Banking at Colorado and teaches at several graduate schools for professional bankers throughout the United States. He serves as faculty advisor to the Graduate School of Bank Investments and Financial Management at the University of South Carolina. He has taught seminars on risk management to bankers in Poland, Hungary, Slovakia, and the Ukraine as part of a U.S. Treasury program to assist private banking in Eastern Europe. Dr. Koch's research and writing focus on bank risk management, performance analysis and improvement, the pricing of financial futures and fixed-income securities, and public finance. He has published in a wide range of academic journals, including the Journal of Finance, Journal of Financial & Quantitative Analysis, Journal of Futures Markets, National Tax Journal, Journal of Banking and Finance, Journal of Fixed Income, Journal of Financial Research, Journal of Macroeconomics, Journal of Portfolio Management, Municipal Finance Journal, and the Journal of Money, Credit and Banking. Dr. Koch has also served as Treasurer of the Financial Management Association and President of the Eastern Finance Association and Southern Finance Association. He has written General Banking curriculum for many state-sponsored banking schools and is a frequently requested seminar leader for the banking industry.

S. Scott MacDonald serves as President and CEO for the Southwestern Graduate School of Banking (SWGSB) Foundation, Director of the Assemblies for Bank Directors, as well as Adjunct Professor of Finance at the Edwin L. Cox School of Business for Southern Methodist University. Dr. MacDonald received his B.A. in economics from the University of Alabama and his Ph.D. from Texas A&M University. He joined the Southern Methodist University faculty in 1997 and began his responsibilities as Director of the SWGSB Foundation in 1998. Prior to joining SMU, he served as Associate Professor of Finance and Director of the School of Applied Banking at Texas Tech University. Dr. MacDonald spends the majority of his time working directly with the financial services industry. In addition to functioning as Director of the SW Graduate School of Banking, he conducts bank director education programs through the Assemblies for Bank Directors and is a frequently requested speaker, seminar leader and strategic planning facilitator. He is also a consultant for various banking organizations. Dr. MacDonald has also served as an expert resource witness before the Texas State Senate. He is a past chairman of the board of directors for Texas Tech Federal Credit Union, an advisory board member of the Independent Bankers Association of Texas Education Council, and past board member of the North Texas Chapter of the Risk Management Association. Dr. MacDonald has authored numerous articles in academic journals, including the Journal of Financial Economics, The Journal of Business, The Journal of Futures Markets, The Review of Futures Markets, Quarterly Journal of Business and Economics, and the Journal of Money, Credit and Banking. He has also written professional curriculum for industry-sponsored seminars and schools in the financial services industry and has been recognized with numerous teaching and research awards.

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