GREETING CARDS AND BANKING

by Steve Brown

Hallmark, the largest greeting card seller in the country, has decided that in order to compete with e-cards and YouTube, it will adapt and change. Just in time for Mother's Day, the company will begin offering recordable greeting cards that allow people to record a 10 second message and a 15 second music clip. The cards will sell for $5.99 each and the battery has enough juice for 220 plays.

We bring this up not only because we found it an interesting twist on an old idea, but it also shows how even a 100 year old company must continually adapt in order to succeed in this ever-changing world. As with greeting cards, the banking industry has also been undergoing massive change as of late.

In fact, troublesome signs in the banking industry right now are about as prevalent as birthday cards are at the Hallmark store. There has been a slowdown in construction, CRE is beginning to weaken, loan losses are soaring and small businesses are coming under greater financial stress (due to higher energy prices and a consumer spending slowdown). All of these issues will need to be corrected, before things finally begin to settle down for community bankers - hopefully in 2009.

Regulatory examination teams have also taken a decidedly different tack with bankers. In an effort to confront credit issues before they get out of hand for the industry, it is clear they have taken the gloves off when it comes to credit and liquidity. Concerns are many and bankers everywhere are telling us examination teams in the field are looking for a robust response and much-improved documentation. To address this, bankers should be in the habit of ordering new loan appraisals to address changes in the marketplace, realistically recognizing losses, taking aggressive steps to deal with problems as they surface and ensuring robust board reporting to keep everyone informed. Increasing delinquencies and losses on CRE have regulators on edge, so bankers will have to move quickly and address things head-on to avoid bigger problems.

As if that weren't enough, for those who missed it, billionaire financier Wilbur Ross has even decided the time is ripe to jump into banking. He has announced plans to set up a $4B fund that will roll up troubled banking institutions (recall that Ross made his fortune by turning around distressed steel and textile companies back in the day). Maybe Ross was listening to Bernanke's comments just a few months ago, when Bernanke stated, "there probably will be some bank failures, although they are likely to be among smaller regional banks that are particularly exposed to falling property markets." Ross doesn't do anything small, so if he is getting into the banking rollup game, it is a good bet there are still some problems deep within the industry.

We don't yet know how well the recordable greeting card will ultimately sell, but the very fact that Hallmark is willing to adapt and change to find out is inspiring. The good news for banks is that despite industry issues, opportunity abounds and out of chaos comes even greater opportunity. Community bankers that adapt to find their own version of the "recordable card" will not only survive this rough economic period, but will thrive. If only Hallmark had a "get your balance sheet well soon" card.

BANK NEWS

BofA

The largest U.S. Bank announced profits dropped for the 3rd straight quarter, due to a $6B increase for loan loss allowance. 1Q net earnings fell 77% to $1.2B. In related news, Moody's lowered BofA's holding company's ratings from "Aa1" to "Aa2."

Nat City

The troubled bank announced that it will raise $7B+ in capital led by Corsair Capital (a JP Morgan Chase related group) to shore up its operations.

Increased Liquidity

The Bank of England said it would allow banks to trade mortgage securities for government bonds, in an effort to improve liquidity and ease market strains.

Private Banking

Union Bank of CA ($55B, CA) launched its "Priority Banking" initiative targeting wealthy households with $100k or more in balances. The mass affluent push will include financial planning, personal bankers, investment and insurance consulting. The sub-focus will be legal, accounting, medical and real estate professionals.

CRE Values

1Q data we have collected shows CRE asset values at banks are down almost 4% from the start of the year, on top of the 6% decrease experienced in 2007. Retail properties were hit the hardest, due to falling debt service coverage stemming from higher vacancies. In addition, effective rents turned negative for the first time since 1989. We will be releasing this and other data, projections and individual market summaries in the next 2 weeks.

Housing

A new Gallup poll finds 53% of people think now is a good time to buy a house. That is down from 58% at the end of last year and from 71% in 2005 and 81% in 2003.