RESTRICTED AREA - DO NOT PROCEED

by Steve Brown

Just a few weeks ago, banking regulators came out with a new final rule telling stressed banks they would be restricted from paying more than the national rate (a simple average of rates paid by all insured depository institutions and branches for which data are available) to attract deposits. The goofy thing about this new rule is that it took a whopping 28 pages of regulatory-legalese to clarify what exactly that meant. We know how busy bankers are and that some may not yet have had time to read the rule, so we decided to provide a summary. This morning, we make use of this tiny space to cram in the relevant portions and keep you in the know (and ensure you don't wander off into any restricted areas).

The rule has been designed to apply to banks that are not "well capitalized" (WC), but wording reiterates the FDIC can impose these restrictions on any institution it determines. Since the rule affects all banks in one way or another and it may lead to calls from regulators to any bank posting a rate that significantly exceeds (more than 75bp above) the national rate, it is worthy for all banks to understand this rule.

In earlier versions, the national rate was kicked around to be calculated based on some spread above Treasuries. After getting industry feedback, the FDIC settled in on using a rate it would calculate and then post on the FDIC website for various maturities. These rates are now available on the FDIC website. (http://www.fdic.gov/regulations/resources/rates/index.html).

The rule is not effective until Jan 1, 2010. That said, a couple of bankers have already told us they have heard whispers from regulators that the rates they were paying were above the national rate and they might want to reconsider lowering them. We are not sure what the banks did, but given the pressure, we would bet they lowered their rates as requested.

The rule indicates that banks which are not WC may not accept deposits from a broker, unless the bank obtains a waiver from the FDIC. "Adequately capitalized" (AC) banks with a waiver may not pay a rate on deposits that significantly exceeds (more than 75bp) the rate paid on deposits of similar maturity in the bank's normal market area (the national rate, unless you can convince the FDIC otherwise) OR the national rate for comparable maturity deposits outside the normal market area (either, or). Meanwhile, AC banks without an FDIC waiver may not pay a rate on deposits that is more than 75bp above the prevailing rates in its own market for ALL deposits (in market and out).

When it comes to "Undercapitalized" (UC) banks, things get even tougher. UC banks may not accept brokered deposits under any circumstances AND they cannot post rates that are higher than 75bp more than rates posted in EITHER the local market OR the national rate (lower of) for ALL deposits.

In a strange quirk, banks that are not WC and do not have an FDIC waiver, should know that the rule categorizes such banks directly as a "deposit broker," if the bank offers rates 75bp higher than prevailing rates in its own market area. Without the waiver, such banks would not be allowed to accept deposits even from themselves if 75bp more than the national or market rates.

The goal of all of this is to limit the rate strained banks can pay to compete for funds within their own market. For stronger banks this is a good thing, since it squeezes out expensive rate payers.

If you are in a high-rate region, consider providing the FDIC data that segments market information based on state, county or MSA and be sure to include rates paid by credit unions in the region. The FDIC has said they will evaluate the information, so it may be worth it to spend the time to see if submitting a request makes sense for bankers operating in more expensive regions.

In our book, any time a bank has to pay a high rate to attract deposits, they are doing something wrong. This rule merely codifies this feeling into regulations that define what exactly those "restricted areas" are. In doing so, the FDIC hopes that all banks will stay away from the dotted yellow lines.

BANK NEWS

Branch M&A

First Financial Bancorp ($3.8B, OH) has entered a deal to purchase 3 branches (including $143mm in deposits) and $200mm in loans from Irwin Union Bank and Trust ($3.5B, IN) for an undisclosed sum.

Fannie/Freddie

The GSEs extended eligibility for mortgages refinances to loans with LTVs up to 125% in order to aid homeowners. Of the 80k already refinanced Fannie and Freddie mortgages, Ã,Â¼ have exceed an LTV of 80%.

Undercapitalized

The top states with the highest level of undercapitalized banks are (from highest to lowest) GA, IL, CA, FL and MI. Not surprisingly, GA has had the largest number of bank failures YTD, with CA, IL and FL following close behind at 6, 6 and 3 respectively.

Deposit Pricing

According to a study by Market Rates Insight, on average, the top 19 US banks priced CDs 42 bps less than all other banks within the first 5 months of this year. As for money market deposits, the gap was 25bps.