BROKERED CD FORUM RECAP

by Steve Brown

Part of our value is to leverage our time and resources for the benefit of all community banks. If you don't mind us saying, we went above and beyond the call of duty by sitting through 2 mind-numbing hours of FDIC roundtable discussion on brokered CDs, so you didn't have to.

On Mar 18th, Sheila Bair chaired a Dodd-Frank mandated roundtable committee in D.C. to discuss and attempt to define the characteristics of core and brokered deposits. This was an attempt to illuminate the benefits and threats that each pose to the banking system. The key issues were around how to define core deposits, available deposits in times of stress, how both core and brokered money play a role in the economy, the potential stimulative economic impact of redefining core deposits and the competitive interplay between large and small banks for deposits. During the course of the Forum, the FDIC explored new ways banks have been obtaining deposits (internet, reciprocal, etc.) and the role of these deposits for liquidity (in times of stress) and in creating "franchise value."

Bill Isaac, former FDIC chair during the 1980's S&L crisis lead the discussion with a cautionary example of how 30Ys ago, lawmakers failed to properly respond to trouble within the banking system. He indicated that if regulators had been given the proper tools back then, they may have been able to avoid or at least soften the landing of even this most recent bubble. As the discussion continued you got the sense that you have seen this movie before, as little new ground was broken.

The conclusions of the roundtable participants were also mixed, as expected. Regulators and academics each put forward statistics and evidence that there was a high correlation between the use of brokered funding and bank failure rates. It was also brought up numerous times that "hot money" helped fuel imprudent growth and was deleterious to franchise value. Meanwhile, providers of brokered funds and internet-focused banks were adamant that such funding provides an important service and increases deposit liquidity - which adds to stability and flexibility in the system. It was also driven home that while it is true that many failed banks had a higher than normal level of brokered funds, correlation does not imply causation (no more than doctors always seem to be the last to touch dead people). You go to the doctor, like going to the brokered market, because you have problems elsewhere. Internet-only banks (like ING Direct) weighed in that the internet is just another delivery channel with the same, or better cross-sell, deposit growth, "stickiness" and other characteristics.

One idea that the Forum seemed to coalesce around was to shift the categorization of "brokered" funds away from a simplistic definition (i.e. term/means of procurement and limitations as a percent of total deposits), to the underlying behavior of the funds. Many on the call also seemed to agree that it is not where you get the funds, but rather more about how they behave. The concept of further defining "volatile" versus "non-volatile" funds also seemed to take hold. The timing of the Forum was particularly apt, as we point out that this was the week that average national rates on internet deposits dipped below the national average of local deposits, thus further blurring the lines. While all of this sounds like an interesting idea, we note that no one surfaced a volatility formula or further defined what "deposit volatility" is and what is appropriate.

What was clear at the end of the session, like most legislative convened panels-further definition, investigation and regulatory review is necessary. We look for the concept of a "volatile" funds definition to possibly take hold, but in a simplistic sense applied within a "rate cap" framework. While volatility of cost and volume can be effectively measured, this will likely prove too hard to regulate and monitor. The bottom line, in our opinion, is that brokered funds will still exist, but banks will be restricted as to their use based on liability and asset structure. While banks will probably be able to exceed a given threshold from time to time, there will have to be a reason (business model, short-term liquidity need, etc.) or restrictions will likely apply. We look to see proposed guidance out of the FDIC by July. Until then, we are on to our next mind numbing forum meeting.

BANK NEWS

More Time

FRB Chair Bernanke sent a letter to Congress, indicating the Fed will not make the Apr 21 deadline to issue final rules limiting interchange fees for debit cards. The Fed said it has received more than 11,000 comment letters and needs more time to review them.

Housing Pressure

S&P reports the average home loan in foreclosure has been delinquent for a record 537 days and 30% of foreclosed loans have not rec'd a payment in over 2Ys.

Free Checking

Analysis finds roughly 64% of large banks offer free checking compared to 90% in 2009.

Small Business

It may sound shocking in this day and age, but 40% of small businesses still donÃ¢Â€Â™t have any online presence whatsoever.

Overdrafts

A study by Moebs finds 90% of overdraft revenue for banks comes from frequent users (those with 10 or more overdrafts in a year), nearly all of which opt-in.