STRANGE, FUN AND INTERESTING

by Steve Brown

You know the recession is getting ugly when you rob your own friends. In a true story we ran across in the press, a man held up two friends at gun point, fleeing with a whopping $60 bucks and one of their cell phones. The good news for police is that not only did the two easily identify this bonehead, but they also knew where he lived and how to find him. You know something is seriously wrong with the gene pool when you stick up your own friends, so we will just leave it at that and move on to the fun of banking. Here are some things we think you will find both interesting and fun to know.

If you want to improve performance at your bank, you might want to start at the very top. A study by Catalyst found companies with three or more female directors produced an average 45% higher return on equity than those with the average board makeup. We can't tell you why, but that is probably because we are from Mars and they are not.

CEOs don't usually move around all that much at banks, but a new study explores the reasons behind those who did over the past year and finds some interesting information. The #1 reason was due to retirement at 40%, followed by resignation at 29%. After those top two reasons, percentages dropped pretty sharply, with 11% leaving to take a new job inside the bank, 8% taking a new job outside the bank, 3% being removed and 2% turning over due to death. We don't know the details behind the final category, but in 7% of the cases the answer was "other."

If you find yourself occasionally wandering around the house late at night or early in the morning because you have insomnia, you are definitely a banker. After all, that is what happens when major crises hit and an industry is thrown into turmoil. A recent survey by Bank Director magazine found that when it comes to audit committee members at least, the primary reasons behind this lack of sleep could be attributed to worries about how well the bank was monitoring enterprise risk management at 31%; followed by unknown risks (25%); regulatory scrutiny (16%); undetected fraud (15%) and inaccurate financial reporting (13%). Counting sheep might not work for a banker under stress because you will probably feel the need to go back and double count them for accuracy, but you might want to give it a shot anyway, the next time you are awake when you don't want to be.

Banks are feeling increased pressure these days, as deposit flows outstrip loan growth. In fact, for the first time since 2007, the industry's core loan to deposit ratio (excluding large time deposits) has fallen below 100%. That increases pressure on NIM, where banks feel obligated to take deposits to retain customer relationships even as loan growth remains tepid. Such low loan growth has also resulted in increased loan competition, as only a small portion of clients needs or wants to take out a loan so spread compression is also evident. Over the next 6 months to 2Ys, these pressures will remain, so look for securities balances to continue to increase until deposit flows subside or loan growth picks up again. At this point, most lenders we talk to say every loan opportunity they see seems to have at least 3 other banks involved and actively competing to win the business.

We also uncovered some interesting facts from a recent RMA survey on ALM practices at community banks. It found that 71% of banks had seen more scrutiny during recent examinations around liquidity and interest rate risk; 66% shocked interest rates by 400bp or more; 29% did not use an interest rate forecast; 38% did not include a cashflow proforma in ALM meetings and 59% did not discuss local economic conditions, despite the fact that most loans were originated locally.

Finally, you might have missed the fact that FASB is considering eliminating the held to maturity (HTM) designation entirely for investment securities. All we can say is haven't banker's seen enough change and have enough on their plates to deal with already without the need for this and the inevitable cascade of "unintended consequences" that will certainly follow?

BANK NEWS

BofA

Warren Buffet steps in to provide BofA with $5B of preferred capital in exchange for warrants around a $7/share strike price (BofA trading today at $7.65). While the move gives a huge boost to confidence, it doesn't help Tier-1 common capital and comes at a hefty cost that we estimate to be about a 10% cost of capital. We say Uncle Warren will end up making at least $1B on this deal.

Deposits

In an effort to help liquidity and market stability, regulators are reportedly negotiating with several large banks to get them to take large institutional deposits in exchange for a reduction of insurance premiums and relief in leverage ratios.

C&I Credit Quality

The credit quality for the $2.5T Shared National Credits (SNC) market improved in 2011 for the 2nd year in a row. Criticized assets represented 13% of SNCs vs. 18% in 2010. Stronger earnings and lower debt service helped cash flow coverage materially increase. In addition, liquidity improved. The Fed found that current loss rates for all rating categories for 2011 have been 89bp.

Mobile Activation

In order to improve security, banks are testing a new system that allows customers to activate and deactivate their debit or ATM card through a mobile app.

Medical Costs

A survey by McKinney finds 30% of employers expect to "definitely" or "probably" stop offering employer sponsored health plans after 2014.