PUSHING BUTTONS IN BANKING

by Steve Brown

What is it with people and buttons? We all like to push them, even if it is not apparent what pushing a button actually does. Consider that research found a "significant percentage" of "close-door" elevator buttons don't do anything when pushed (they have been deactivated by the owner or stopped operating); nearly all of the little buttons at crosswalks that signal "walk" don't do anything any more (computers now handle that job, but the cost of removing the buttons is too much for cities to deal with, so they just leave them); and at least 75% of all office thermostats are just there for looks (and are actually not hooked up to anything). Yet, people stand there staring or looking around, as they repeatedly poke at any given button in front of them - somehow believing that doing so will cause a magical light to work, some doors to close or an office to suddenly become comfortable. We hope this pushes your buttons today, as we push our discussion into banking. Low interest rates, elevated regulatory costs, increased competition and greater asset prepayments are all factors putting pressure on community banks in particular. So much so, in fact, that some have started work to find a partner and sell out (93% of deals announced since 2011 are for institutions under $1B), while others have decided to hunker down and find a way through this difficult period. For those continuing to work through this period, caution is running high about taking any sort of credit risk, amid an uncertain economic recovery. Unemployment is high, housing is in the tank and those fundamental issues, combined with the list outlined above have many bankers feeling less than optimistic about their ability to generate reasonable profits. As pressure mounts, some bankers have extended asset maturities. That has led the Fed to name this an area of focus during exams, as regulators worry banks are extending duration in a low rate environment that could result in a negative impact when rates rise. Proper structuring of both assets and liabilities is critical at this juncture, lending activity begins to appear. To help protect capital from the impact of rising rates (and other comprehensive income), some banks have begun to move longer duration securities into their held to maturity (HTM) portfolios or to purchase loans (not subject to OCI). These strategies can make sense, but here again; bankers also need to stress test the impact to capital and liquidity before pushing this button. Industry conditions are tough, lending volumes remain low, real estate lending remains weak and competition is high, that is a given. The good news, though, is that credit issues are subsiding and the industry is clearly healing itself, albeit slowly. Our advice given the state of the industry right now is to stick closely to the fundamentals. Keep steadily pushing down your funding costs (banks under $1B still pay about 21bp higher to fund themselves than larger banks according to the most recent FDIC data), as you protect your best clients on the asset side. Then, focus on reducing your efficiency ratio wherever and whenever possible (banks under $1B are about 22% less efficient than larger banks). These key areas are fundamental to a healthy bank and they won't come without significant and ongoing efforts for your entire management team. Unlike the ubiquitous non-working cross walk button, pushing these buttons at your bank, even if they take time to work, will deliver benefits.

Related Links:

Exam Guidance

BANK NEWS

Closed (12)

Regulators closed Global Commerce Bank ($144mm, GA) and sold it to Metro City Bank ($388mm, GA). Metro assumed 3 branches, 55% of the assets and all deposits (no premium).

Exam Guidance

The Fed issued guidance on Friday to its examiners over when they should consider upgrading a bank under $10B in size. The short answer is, improved core earnings, a material decline in non-performing assets, sufficient liquidity position, a strong risk management framework (including managed interest rate risk) and an improved, and sufficient capital position. While nothing new, the 2 page missive can be found by folling the Exam Guidance link in our related links section below.

Out of Business

After not being able to find a suitable buyer, Aurora Bank FSB ($4.3B, DE) will close its correspondent lending unit due to profitability.

Call Report Changes

The FFIEC approved changes to the Call Report that will take effect over the next 2 quarters. The modifications impact savings associations that used to file TFRs and will now file Call Reports. About 6 items have changed, as it relates to the instructions and input of some capital, loan and deposit line items.

Investment Advisory

Research finds the percentage of community banks that have investment programs in their branches has remained 20% since 1994.

SAR Confidential

FINCEN sent out an advisory letter reminding banks about the need to keep Suspicious Activity Reports confidential, particularly as it relates to civil litigation.

Still Ugly

A report from CoreLogic indicates 22.8% of all residential properties with a mortgage had negative equity at the end of 4Q, up from 22.1% in 3Q. In addition, 2.5mm people have less than 5% equity. Added together it means 33% of borrowers would need to put in more money to sell their home.

Theft

The FTC indicates it and other agencies received 1.8mm consumer complaints of financial scams last year, up from 1.4mm in 2010. These activities cost Americans $1.5B and identity theft remained the top category (5Ys running) at 15% of all complaints last year.