THE STATUS OF LENDING ACTIVITIES

by Steve Brown

A study by the Brookings Institution of the largest 100 metropolitan areas finds housing costs an average of 2.4x more near a high scoring public school than a low scoring school (about $11,000 more per year). In addition, home values are $205,000 higher on average in the neighborhoods of high scoring vs. low scoring schools and those homes have 1.5 more rooms. Finally, the study found 60% of high school dropouts came from the bottom 20% of families by income and 70% of students enrolled at the most competitive universities in the country came from the top quintile of parental socio-economic status. We found these data points interesting, so we share them this morning. In an interesting twist for the banking industry, it was recently made public that following a shareholder lawsuit over some bad loans, the board of Synovus Bank has agreed to no longer participate in the approval of any loans the bank is considering. That is certainly an odd twist for most community banks, as nearly all we know have a director's loan committee where directors are commonly included in such decisions. Upon reviewing regulatory materials on the roles and responsibilities of directors, it is clear bank regulators do require the board to play various roles when it comes to loan activity. But does that mean they actually need to approve specific loans? The technical answer is no in most cases, but you be the judge. Under the regulations, bank directors are responsible for overseeing the loan review process (usually through audit) and must have a loan committee set up to ensure management handles credit risk in compliance with policies. The committee must verify management is following appropriate procedures to recognize adverse trends, to identify problems in the loan portfolio early, to take corrective actions and to maintain an adequate allowance for loan and lease losses. Finally, the committee must make sure risk controls are in place to ensure compliance with loan related or applicable laws and regulations. As can be seen, so far nothing above absolutely requires that directors evaluate or approve specific loans (or make credit decisions), although this is quite common and especially so when it comes to larger dollar amounts. The exception of course relates to loans to insiders to comply with Regulation O and securities exchange corporate governance rules, among others. However, regulatory actions following bank failure have shown directors that served on loan committees and approved loans may be targeted. A director that recommends a loan for approval vs. actually approves it can blur the lines between directors and management. In a failed bank situation, that may increase the possibility of regulatory action. That said, it is also quite difficult as a director to try and avoid responsibility for the business unit that typically produces the most revenue. In short, it is critical that directors set the tone from the top with strong policies and procedures. All directors should know how the policies apply, no matter how they are personally involved in the process. Such key factors as credit quality, concentrations, laws, regulations, loan limits, risk appetite, training and others all come into play. In addition, directors that have information about the borrower should share what they legally can to enhance the credit decision making process and help the lending team. As you conduct your own lending process analysis to determine whether it is high or low scoring, it is good to know that the law says credit decisions are generally subject to the business judgment rule. In short, directors are presumed to have taken action in the best interest of the bank, with the care that an ordinary prudent person would exercise in similar circumstances. Take care when lending and be prudent, but don't be afraid to get involved regardless of your lending socio status.

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BANK NEWS

M&A

Investar Bank ($342mm, LA) will buy First Community Bank ($110mm, LA) for an undisclosed sum.

Business Survey

A quarterly survey by the National Association for Business Economists shows about 50% of respondents expect GDP to grow 2% to 4% this year, up from only 36% just three months ago. Unfortunately for banks, on the lending side, only 40% expect their business to increase capital spending this year, down from 52% three months ago.

Competition

A report by AlixPartners finds 92% of the 25 largest banks offer some kind of mobile payment and 48% allow mobile check deposit.

Customer Movement

A survey by RBS Citizens finds 79% of middle market companies (revenues $5mm and up) are looking at acquisitions this year and 24% are already involved in one.

IT Spending

Gartner predicts technology spending in the banking sector will rise 3.5% from 2012 levels, as banks increase their focus on lending, trading, risk and payments.

Crackdown Coming

Regulators have finally said they will focus efforts soon on reforming the shadow banking sector, as they complete the financial services overhaul in the next 2Ys.

Mortgage Buying

A survey of major investors by JPMorgan finds 67% expect the Fed will continue to buy mortgages until the 1Q of 2014 (47%) or the 2Q (20%). The rest expect purchases to end sometime this year.

Municipial Bonds

Analysis by JPMorgan finds AAA rated municipal issuance has fallen from 56% of the primary market in 2007 to only 11% today (limited use of insurance). Further, AA and A rated bonds have increased to 25% and 12% of annual issuance, respectively. This is one key reason regulators now require bankers to do more credit analysis on the underlying issuers to stay on top of things.