

PSST - A SECRET WORTH SHARING

by [Steve Brown](#)

We are nostalgic for that which we can no longer have. We remember the Secret chocolate bar from Nestle. The commercial went like this: "You can't trust anyone to keep a secret". That TV advertisement ran in 1990 and the bar had a Walnut Whip center. Nestle's Secret was a popular choice until the complex and costly production process led to its eventual demise. We are also nostalgic for that which we can no longer have in banking - long-term customer relationships, better credit quality borrowers and fee income. Are they gone forever? Did the intense competition and low interest rates make sticky borrowers and fees the dodo bird of the banking industry? Not exactly. Many banks continue to add loan totals and win business in a very competitive environment. A number of regional and community banks have grown total loan volumes over 10% from 2011 to 2012. Some banks have increased fee income as a percentage of total revenue. One common factor for many of these same banks is also their use of interest rate swaps.

When interest rates were higher, loan growth was robust and competition was less intense. In those bygone days, banks could rely on fees from deposit accounts, overdrafts and loan origination (often on construction loans). While relationships were important, if a bank lost a borrower to a competitor, another borrower was already waiting in the lobby to apply for a new loan. Things are different today, with rates low, loan competition intense, scant opportunity to produce fee revenue and fewer credit-worthy borrowers in the market. Furthermore, a loan lost to competitor with the right prepayment provision is now potentially a relationship that is lost for a decade (too expensive for the customer to switch). One solution for community banks is to use hedging as a way to lock in borrowers for longer terms. Doing so eliminates the threat of loan poaching and it gives your customer facing teams plenty of time to cross sell other products and services (modifying customer behavior and making them want to stay with your bank because it has become a key relationship over time). At the same time, hedging can be used to generate much needed fees for the bank - as much as 50 to 150bps of the loan amount. For banks seeking to boost fee income, this could be worth exploring and we can show you how to do it. These are just two reasons why national and larger regional banks are aggressively pricing long-term fixed rate loans using hedging. Banks that use hedging also lock in long-term relationships, eliminate competition and generate much needed fees. Community banks have used our hedging program to do all of this, but with a few twists - no requirement for derivative accounting and no ISDA documentation. If your bank wants to capture more relationships, book more loans, defend existing customers and generate more fee income, we can help. When we think back fondly about the Secret bar, we wonder whether we have been sucked in by what psychologists call "rosy retrospection," where past events are recalled more positively than they actually were at the time. We do remember now that the Secret was a little too sweet and quickly made our thighs tight in our pants. A sentimental longing for the past is not always going to deliver results, so strategy is critical. The environment has changed and banks must continually learn and adapt.

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BANK NEWS

M&A

Guaranty Financial (\$1.2B, WI) has sold its mortgage company (Shelter Mortgage) to private equity firm CIVC Partners (IL) for an undisclosed sum.

Hacked

The Federal Reserve said its Emergency Communications System was hacked (purportedly by activist group Anonymous) and information was stolen on about 4,600 bankers and then posted on the internet. Stolen information included mailing addresses, business phone, mobile, business email and fax. In addition, for those registrants that had provided it, home phone and personal emails were also disclosed.

Massive Theft

A crime ring consisting of 18 people in New Jersey has been arrested and charged with creating 7,000 fake identities and 25,000 credit cards to create 80 sham companies that then took out loans of \$200mm that were never repaid.

Huge Fine

Fine: Royal Bank of Scotland (UK) was fined \$612mm for manipulating interest rates (Libor), the third bank so far (UBS paid \$1.5B and Barclays paid \$454mm). The fine breaks down as \$325mm to the CFTC, \$150mm to the Department of Justice and \$137mm to the UK's Financial Services Authority.

Jail Time

SVP and Chief Lending Officer Gregory Bell has pled guilty to bank fraud, money laundering and making improper loans in an effort to save failed bank New Frontier Bank (CO) from going under. Bell reportedly lent \$20mm to eight borrowers who then used some of the money to buy stock in the company. Bell faces up to 30Ys for each count of bank fraud and 20Ys for money laundering.

Funding Costs

Analysis by Go Banking Rates of over 4,000 banks and credit unions finds states with the highest average rate by APY for a savings account are: OK (0.34%), RI (0.32%), AL (0.29%), NC (0.29%) and ND (0.28%). Meanwhile, states with the lowest average rate are: AZ (0.12%), SD (0.15%), NV (0.15%), MT (0.15%) and IN (0.15%).

Fed Change

Two Senators have introduced a bill that would change the Fed's dual mandate (inflation and unemployment) to a single mandate focused on price stability.

Online Banking

A report by comScore finds 45% of internet users in the US have accessed bank websites.

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