Turn on Your Electronic Devices for Capital

by Steve Brown

Between the tight seating, grumpy passengers and stale air, there are few comforts on an airplane; however, we no longer have to turn off music, videos or electronic books during take offs and landings. It is amazing that for all these years an errant iPod could fritz out the navigating equipment on a great big jet airplane. It is great we have solved that issue, but we wonder why such devices are fine to use at 10,000 feet (which is not that far off the ground) if you are taking off from an airport like Denver or Albuquerque. What would happen when taking off in Quito, Ecuador, which is already at an altitude of 9,350 feet? Mysteries remain, but in easing the restriction, the FAA stipulates that airplanes must have proper protection from electronic interference if they are going to allow such devices during takeoff and landing. Larger devices, like laptops, will continue to be restricted because they could injure passengers if they were to fly about the cabin in a rough maneuver. It is true that we would rather be hit with an iPad than a laptop, but then who decides the cut-off size?

This is the difficulty of broad-based regulations and restrictions, both in enacting and in easing them. We wrote not too long ago about crowdfunding and how it seemed an unlikely resource for banks to raise capital. Yet, there is another resource for raising capital that banks are beginning to explore, and this is the ability to advertise private offerings to the general public. This has come about due to the easing of another restriction, the 80Y old ban on advertising for private offerings by hedge funds, buyout firms, startups or existing small firms seeking capital.

Worries remain as things get underway here, but at a high level, in order to invest in private offerings it is necessary to be an accredited investor. That is defined by having a net worth of at least $1mm excluding an individual's primary residence or annual income of $200,000 in the previous 2Ys. These qualifications don't guarantee sophistication of course, but would probably keep the truly na?ve away. It's estimated that there are about 7.6mm households in the US who qualify as accredited investors. Given this relatively small number of qualified investors, it seems unlikely that this advertising with dominate the airwaves and would probably be more targeted. Supporters of the rule say it brings regulations more in line with modern financial markets.

Hedge funds have expressed the most interest in using advertising to find new investors, as they are typically the least geographically restricted. This avenue is also coming into focus with community banks that operate in small markets or rural areas. For these banks, once the usual sources for raising capital like board members and local investors have been exhausted, the ability to grow can be impeded. The ability to broaden the pool of interested parties to the entire country might be very helpful and bring in needed capital to grow.

For banks that might consider advertising private offerings to a broader audience, we recommend that you proceed carefully and be certain to follow all the compliance hurdles like disclosures to investors. In addition, know something about your new investors, especially if in the past all your investors have been close friends of the bank (because new investors can also be quite vocal at times). There is reputational risk working with investors who may not understand the long term nature of private investments as well, so get professional help. The good news is that this avenue could open new opportunities for community banks to raise capital, so it is positive from that perspective.

BANK NEWS

M&A

Horizon Bank ($1.8B IN) will buy Summit Community Bank ($163mm, MI) for $18.4mm in cash and stock.

M&A

Fidelity Bank ($250mm, TX) will buy First National Bank of Byers ($99mm, TX) for an undisclosed sum.

M&A

First Bank ($262mm, AR) will buy First Community Bank of Crawford County ($74mm, AR) for an undisclosed sum.

Branch Closures

First Mariner Bank ($1.3B, MD) will close two branches as it adjusts to more of its customers doing business online or through mobile channels.

Cyber Risk

Trend Micro reports malicious software (malware) focused on stealing online banking credentials reached 200k in 3Q, the highest level in 11Ys. By country the top three in new infections were the US (23%), Brazil (16%) and Japan (12%).

Regulation

The CFPB has begun to collect complaints on payday lending products, saying such products can push consumers into a cycle of indebtedness. The CFPB is focused on loose underwriting standards, high costs and risky loan structures as possible contributing factors to consumers' sustained use of the products.

Regulation

The OCC issued standards for outside consultants that come into a bank to do work related to an enforcement action around AML, SARs, consumer protection violations, fraud and management deficiencies. The standards require consultants be independent, have proper due diligence and be qualified to do the work required. The OCC said it will also review the consultant's final report to decide whether further outside work is required.

Branches

An Accenture study finds 32% of US bank customers use mobile banking at least 1x per month, but 80% say they expect to visit branches just as much 5Ys from now as they do currently. We should note we don't believe the second point and reiterate it is just a projection that doesn't match the real trends banks are experiencing.