Kissing Frogs But Finding No Prince Charming

by Steve Brown

Lots of strange things can happen when a princess kisses a frog. We cannot imagine kissing a frog ourselves, but then again we are not aware of any royal bloodlines either so maybe these are linked. As many childhood stories go, the princess puckers up and kisses the frog, only to see flashing lights, stars and other pyrotechnics as the amphibian metamorphoses into Prince Charming. That never gets old we have to say.

Our congressional representatives must also really like this story because so many seem to so often act like young children. They have no qualms about tucking a special amendment tadpole into an essential funding bill to get their way.

Look no further than a provision that has been slipped into the most recent highway funding bill. That provision would cut the 6% dividend the Fed pays member banks that has been in existence for 100 years. Leave it to Congress to say, "Hey, there is $17B sitting over there at the banks and since they are banks and we had a credit crisis some years back, maybe they should pay for the highway system." Huh, what?

To get a better handle on this, it is important to understand what this dividend really is. You see, when banks join the Fed system, they have to buy stock equal to 6% of assets. That stock cannot be sold and it does not change in price. So, to keep banks in the fold and encourage more to join, the Fed has paid a 6% dividend for some time. Now Congress wants to cut that down to 1.5% for any bank that has more than $1B in assets.

Maybe they are thinking only of themselves, maybe they don't care about the banking system or maybe they just don't think something that has been in place 100 years matters. It is hard to tell, but it is certainly shocking that this was all done apparently without any study of its impact, without any hearings and without even talking to the Fed to get some insight.

We are not against paying for services the government provides and readily acknowledge that bankers are among the millions of drivers nationwide using the highway system. In fact, we took it upon ourselves to do the math and find that there are about 318,860,000 people in the US. Of these, some 2,042,386 are employees of banks according to the Q2 data or about 0.64% of the population. While some of these bankers may walk to work, we say ignore that and stick it to all of them anyway by charging this industry that portion of the highway bill.

A bit more research uncovers a CBO estimate that shows $9.8B needs to be transferred from Treasury to the Highway Trust Fund to support continued spending on highways through 2024. So, by using our analysis above and ignoring entirely those bankers that are environmentally conscious and walk or bike to work, we uncover what the true bill should be - bankers should cough up a whopping $62,771,695 as an industry. Given there are 6,348 FDIC insured institutions in the country as of the end of Q2, that means the straight math is about $9,888 per bank - nowhere close to the $17B Congress is trying to grab.

Certainly, the highway system has to be paid for and we know

that the gas tax isn't getting it done anymore since so many people have gone green and are driving electric or hybrid cars on the road. We would argue though, that doesn't mean it is time for Congress to just stick it to the banks. If Congress knew anything financial, they would recognize community banks not only play a huge role in our country (support most lending to agriculture and small business industries), but they are also reeling from heavy regulation, low interest rates and extreme competition and cannot handle any more. It will certainly have unintended consequences, exacerbate extreme pressure on community banks and likely push many more out of their very existence. Maybe our princess was onto something or maybe she was just nutty about kissing frogs, but we sure hope Congress wakes up and realizes that taking this action won't deliver the flashing lights and metamorphoses they desire.

BANK NEWS

Lending Costs

The new proposed FDIC assessment would increase costs for banks under $10B in assets in certain areas. One of the biggest hits could come from those banks that do construction and development lending, because the rules require banks to calculate each loan category as a percentage of assets and then multiply each one by a charge off rate provided by the FDIC (almost 18x higher than the rate for agriculture business lending for instance - 4.50% vs. 0.24%). Another area that could be costly is for banks seeing strong loan growth. Here, the proposal would increase assessment levels using a multiplier based on year over year asset growth, but excluding growth related to M&A. The investment bankers must be licking their chops, as this odd carve out will likely drive faster industry consolidation.

Apple Loans

Apple has selected Citizens Bank ($107B, RI) to provide financing (24-month, unsecured installment loans for an APR of 11.99% to 19.99%) to customers seeking to upgrade to the latest iPhone (starts at $648).

M&A Activity

1) Bank of Montreal (Canada) will acquire GE's transportation finance business (has about $9B in earning assets) for an undisclosed sum.

Oil Risk

Bloomberg reports Goldman Sachs has updated and slashed its projections for oil prices, warning that $20 could be possible.

Business Access

Facebook said it has expanded its design for small business pages, improved mobile design and upgraded features for small businesses in an effort to help consumers more easily connect with businesses through its platform. Facebook now has more than 45mm active business pages, so community banks may want to take a look to see whether or not this is an opportunity.