

# AMERICAN BANKER<sup>®</sup>

THE FINANCIAL SERVICES DAILY

Wednesday, November 3, 2008

## 'Need' Becomes Relative With Treasury Cash in Play

■ BY ALAN KLINE

Like hundreds of other banks, International Bancshares Corp. in Laredo, Tex., is weighing whether to apply for the Treasury Department's Capital Purchase Program.

The \$11.5 billion-asset company is concerned that, if it does not bid for the \$200 million of Treasury money for which it is eligible, it could lose business to banks that do.

"Even though we don't need the capital, all these other banks are going to be that much better capitalized," said Jonathan Nixon, International's general counsel. "Bank of America is taking it, and now they are going to be supercapitalized, and we are competing against them every day."

Competition is just one issue that executives at small and regional banks are mulling as they assess the pros and cons of seeking a share of the \$250 billion the government is investing in exchange for preferred shares.

Daniel Blanton, the president and chief executive of the \$1.4 billion-asset Southeastern Bank Financial Corp. in Augusta, Ga., said he worries that if his two-bank holding company — which is already well-capitalized — decides against accepting Treasury money, its capital ratios will look artificially low in relation to peers', and examiners will take notice.

"If regulators encourage you to take it and you don't, how are they going to view it?" he asked. "Are they going to redefine what 'capital adequacy' means?"

Customer reaction is also on his mind. "They might say, 'If you take the capital, that means you're all in trouble,'" he said. "Or, they might say, 'If you don't take it, you're all in trouble. It's a Catch-22.'"



"In or out, no one wants to make a mistake," Kafafian says.

Southeastern is eligible for up to \$30 million of Treasury money, and Mr. Blanton said his company is preparing the paperwork in case it decides to apply by the Nov. 14 deadline.

So far, about three-dozen banking companies have received at least preliminary approval for the Treasury funds, and many others have said they either have applications pending or intend to file soon.

But countless others are still asking whether they want the government owning stakes in their banks. Can they live with the strings the Treasury is attaching to its money, and those it might attach? If they do add capital through the Treasury program, is there enough loan demand in their markets to safely deploy it? And if they opt not to take the money now — because they do not need it — will they regret it a year or two later, when raising capital might be more expensive?

"There is still a lot of confusion among

community bankers," said Robert E. Kafafian, the president and CEO of The Kafafian Group, Inc., a community bank consulting firm in Parsippany, N.J. "In or out, no one wants to make a mistake."

The decisions are so weighty that the American Bankers Association has asked Treasury Secretary Henry Paulson to extend the Nov. 14 deadline.

"In many cases, [bankers] see the value in the program to the economy and their communities, but they should not be required to make this critical decision that could affect the future of their banks in such a tight time frame and with so many uncertainties," ABA president and CEO Edward L. Yingling wrote in an Oct. 30 letter to Mr. Paulson, which was copied to the heads of all the bank regulatory agencies.

Some banks seeking Treasury money will not necessarily get it because they might be viewed as too weak.

But most banks and thrifts are healthy enough to at least be considered, and banking consultants and attorneys are being deluged with calls and e-mails seeking advice.

For clients on the fence, Mr. Kafafian is urging participation.

Banks that sell shares to the government will pay a dividend rate of 5% for the first five years and 9% afterward. "I'm telling them that they are never going to get capital this inexpensively," Mr. Kafafian said, "and if they don't need it, they can just pay it back."

Chip MacDonald, a partner in the capital markets group at the law firm Jones Day, said bankers should consider what their capital ratios will look like if they choose

not to participate. "Regulators often base their capital evaluations on peer comparisons," he said. If a lot of banks sell shares to the Treasury "and you don't, even though you're currently well capitalized, what are you going to look like on a peer-comparison basis?"

But Sanford Brown, the managing partner in Bracewell & Giuliani LLP's Dallas office, said some of his clients, feeling pressured to apply for the Treasury funds, are seeking his help in explaining to shareholders and customers why they should not.

"The calls we got when this first came out were about how to get access to the money," he said. "People call now and say, 'I don't want this, but I can't document the reasons why I don't want it ...' We are starting to analyze and document why it is prudent not to do this."

Cullen/Frost Bankers in San Antonio is in that camp. The \$14.1 billion-asset company announced Friday that, after some deliberation, it had decided not to apply for Treasury funds because it just does not need the money.

"As we have in the past, we expect that our business and its earnings, coupled with our strong capital base, will provide the necessary capital to continue our growth," chairman and CEO Dick Evans said in a press release.

The \$1.1 billion-asset Cape Bancorp Inc. in Cape May Court House, N.J., also decided against participating. It raised \$78 million when it converted from a mutual thrift to a public company in January. It also completed a simultaneous acquisition, buy-

ing Boardwalk Bancorp Inc. in Linwood, N.J., for \$101 million.

Cape's 13.79% risk-based capital ratio makes it "a well-capitalized institution," said

## Cross-Currents Bedevil Banks on Treasury Cash

Herbert L. Hornsby Jr., the president and CEO. "We looked at our marketplace and the potential to quickly grow past the capital that we already have, and we don't feel in this environment there is a good reason to take on more capital, particularly capital with the strings that the government, perhaps appropriately, has put on it."



**Decisions:** Cullen/Frost generates enough capital from earnings, says Evans, left. Could regulators redefine "capital adequacy?" Blanton asks.



Nevertheless, he said, the company does worry about the risks of opting not to take part.

"The biggest risk to saying 'no' is, 'What is the market impression of the whole thing?'" he said. "Because it seems like everyone is getting in line...like somebody's giving away candy."

The \$2.1 billion-asset Community Bankshares Inc. in Greenwood Village, Colo., applied for the money last week because it is feeling regulatory pressure to increase its capital, said Donald Woods, its chairman, president, and CEO.

"There is clearly pressure from the regulatory bodies to increase the amount of risk-based capital," Mr. Woods said. "And this is an opportunity to raise relatively inexpensive capital."

Mr. Woods said his company's capital ratio is slightly above 11% but that, if it is granted the full amount requested, it would have 14% to 15% of risk-based capital.

Though it was not the primary driver, he said, competition also motivated his company to participate.

"There is some peer pressure in the industry to get that extra capital," he said. "I don't want to be the only bank in the neighborhood that doesn't have it."

The program's terms and conditions could very well change, Mr. Woods said, as policymakers debate the program's implementation and even its purpose.

"I would be naïve to think there is not going to be some unintended consequences that we don't know of yet," he said. "But I view them as another significant shareholder that takes a large

ownership position in your bank. They have some rights to influence the decisions of management; as long as it's not too onerous, I don't view it as a big problem."

**Robert Barba, Bonnie McGeer, and Marissa Fajt contributed to this story.**