

FIG Partners  
West Coast Bank CEO Forum

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California Department of Financial Institutions

# Topics for Discussion

1. Update on banking industry demographics and condition
2. Is the community banking business model at risk? (Revisiting FIG 2011)
3. Where do we go from here with bank regulation and supervision? (Revisiting FIG 2011)
4. Observations on the economy, credit conditions, risk factors

# State / National Bank Comparison

## California Headquartered Institutions (as of 12/31/11)

	<u># State</u>	<u>% of total</u>	<u># Natl</u>	<u>% of total</u>
< \$100MM	19	10%	5	10%
\$100MM - \$500MM	107	58%	33	67%
\$500MM - \$2B	40	22%	4	8%
\$2B - \$10B	14	8%	2	4%
Over \$10B	<u>6</u>	<u>3%</u>	<u>5</u>	<u>10%</u>
Total	186	100%	49	100%

# State / National Bank Comparison

## Total Asset Size (as of 12/31/11)

	<u>\$ State</u>	<u>% of total</u>	<u>\$ Natl</u>	<u>% of total</u>
< \$100MM	1.3	0%	0.3	0%
\$100MM - \$500MM	24.8	9%	6.6	4%
\$500MM - \$2B	39.0	14%	3.9	2%
\$2B - \$10B	54.0	20%	8.0	4%
\$10B and >	<u>152.4</u>	<u>56%</u>	<u>159.3</u>	<u>89%</u>
Total	271.6	100%	178.1	100%

Total assets in billions of dollars

# Changes Among State Banks in 2011

## Dollar Amounts in Thousands

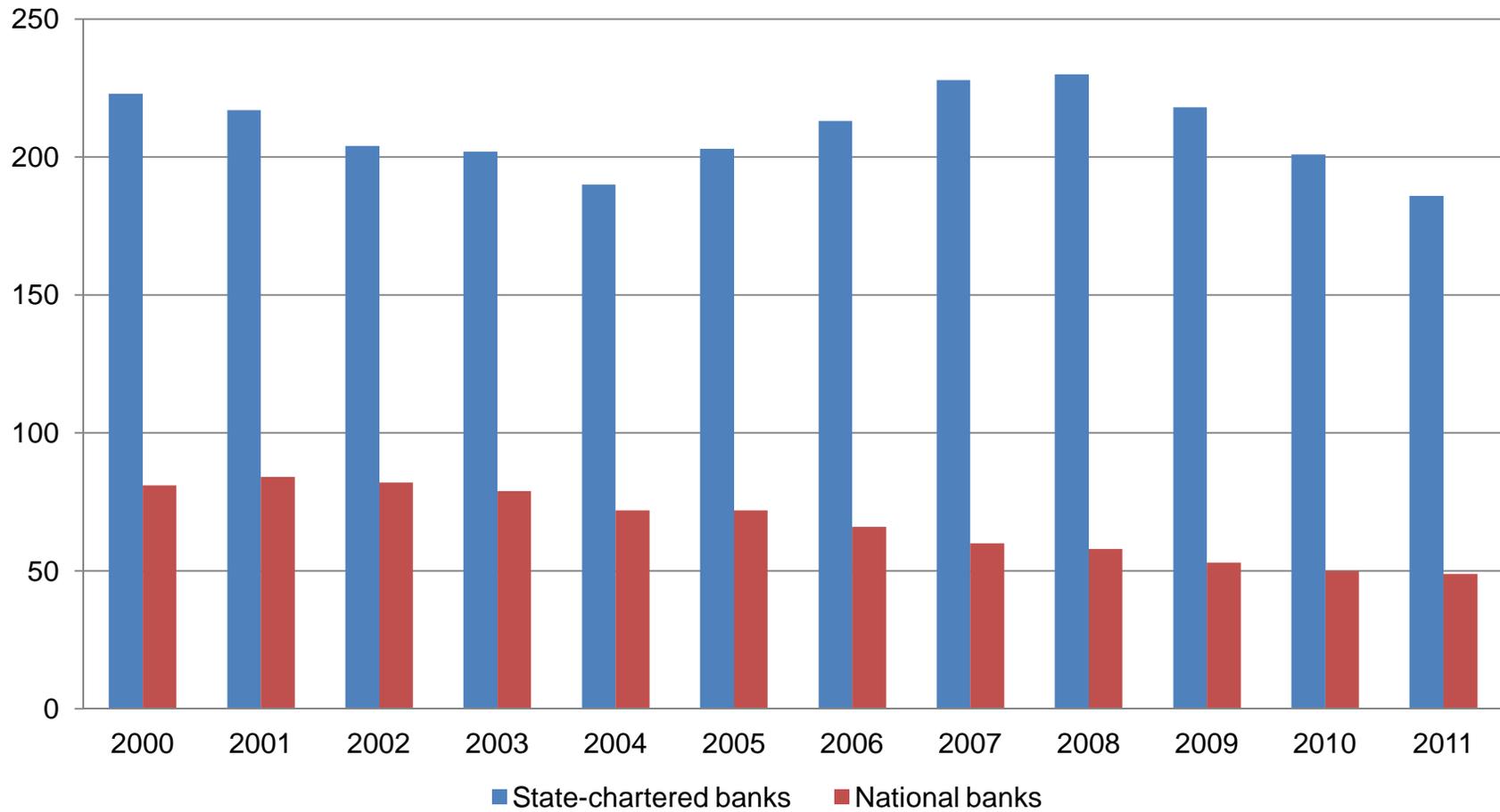
	#	\$
<b><u>Number of state banks and total assets as of 1/1/11</u></b>	<b><u>201</u></b>	<b><u>255,101,811</u></b>
# Failed	(2)	(449,003)
# Merged out of business	(12)	(6,298,848)
# Converted to national charter	0	0
# Ceased doing business	(1)	(116,897)
# Opened	0	0
# Converted to state charter	0	0
State banks that acquired other banks	8	5,913,894
<u>State banks that did not acquire other banks</u>	<u>178</u>	<u>17,442,787</u>
<b>Number of state banks and total assets as of 12/31/11</b>	<b>186</b>	<b>271,593,744</b>
<b>Net change:</b>	<b>(15)</b>	<b>16,491,933</b>

# Changes Among State Banks 2005 – 2011

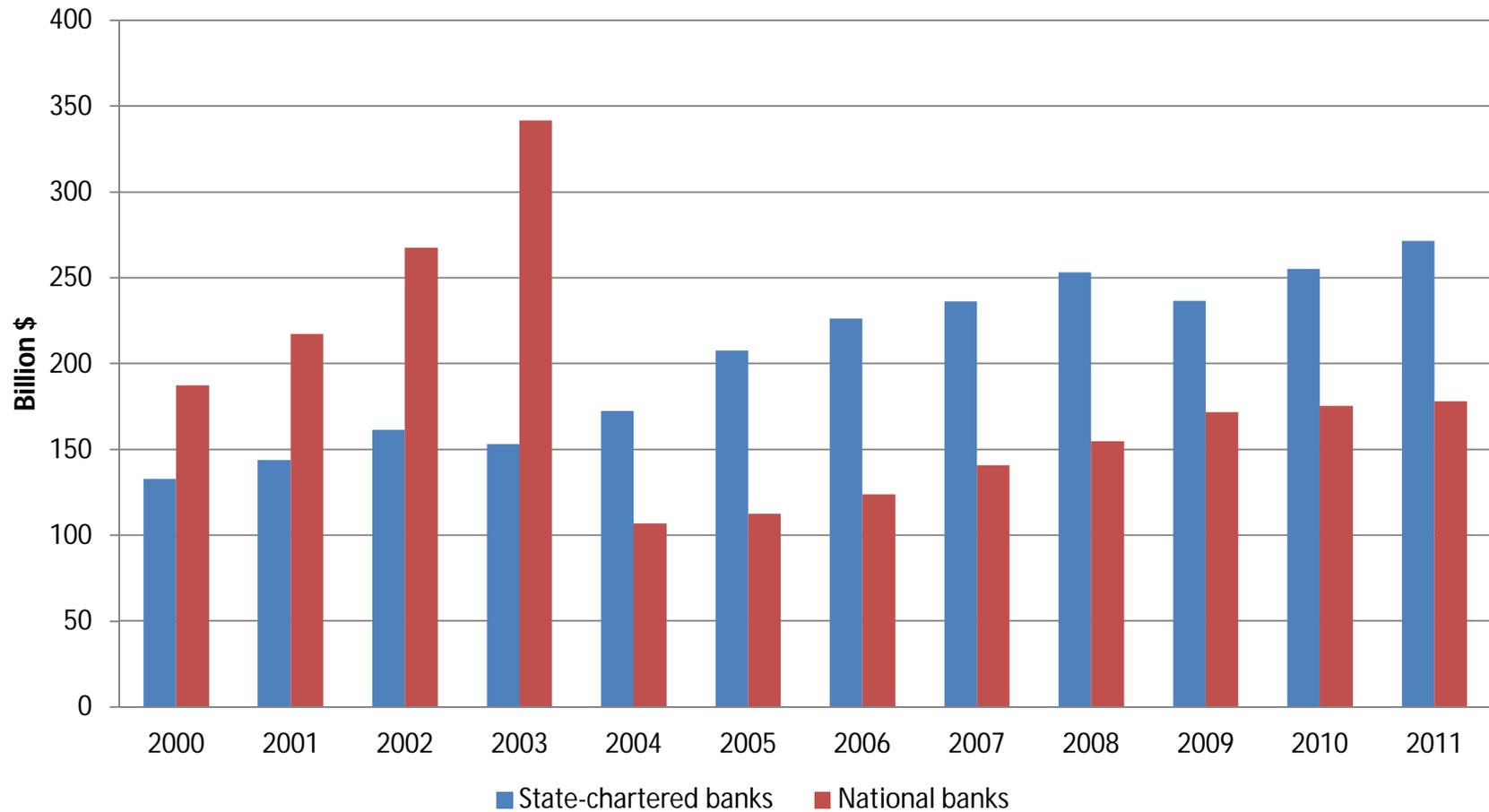
## Dollar Amounts in Thousands

	#	\$
<b><u>Number of state banks and total assets as of 1/1/05</u></b>	<b><u>189</u></b>	<b><u>172,470,243</u></b>
# Failed	(23)	(33,137,711)
# Merged out of business	(54)	(22,875,793)
# Converted to national charter	(2)	(4,456,770)
# Ceased doing business	(3)	(7,783,021)
# Opened	71	48,246,299
# Converted to state charter	8	15,212,447
State banks that acquired other banks	23	66,661,677
<u>State banks that did not acquire other banks</u>	<u>107</u>	<u>37,256,373</u>
<b>Number of state banks and total assets as of 12/31/10</b>	<b>186</b>	<b>271,593,744</b>
<b>Net change:</b>	<b>(3)</b>	<b>99,123,501</b>

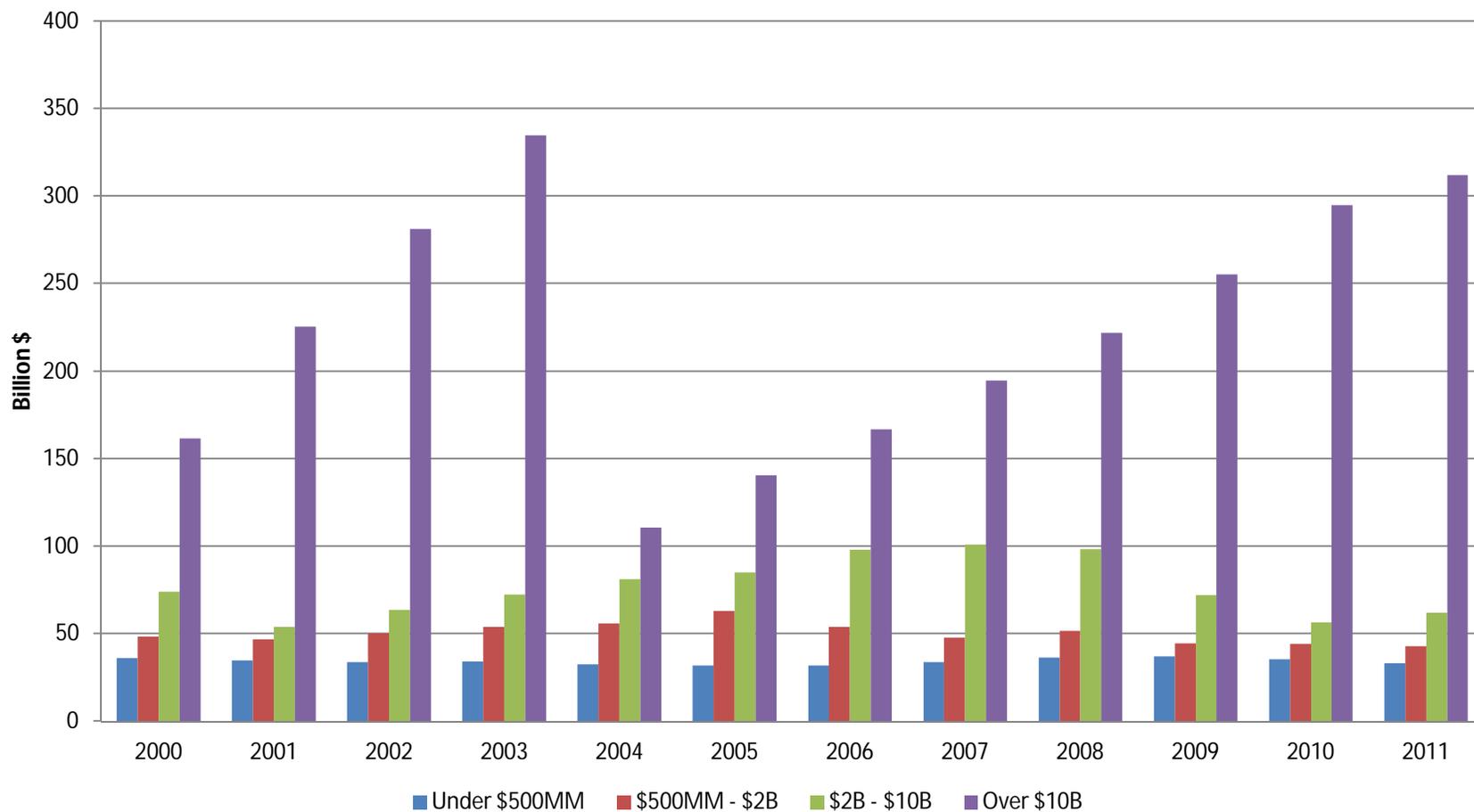
# Number of California Headquartered Banks By Charter Type



# Total Assets of California Headquartered Banks By Charter Type

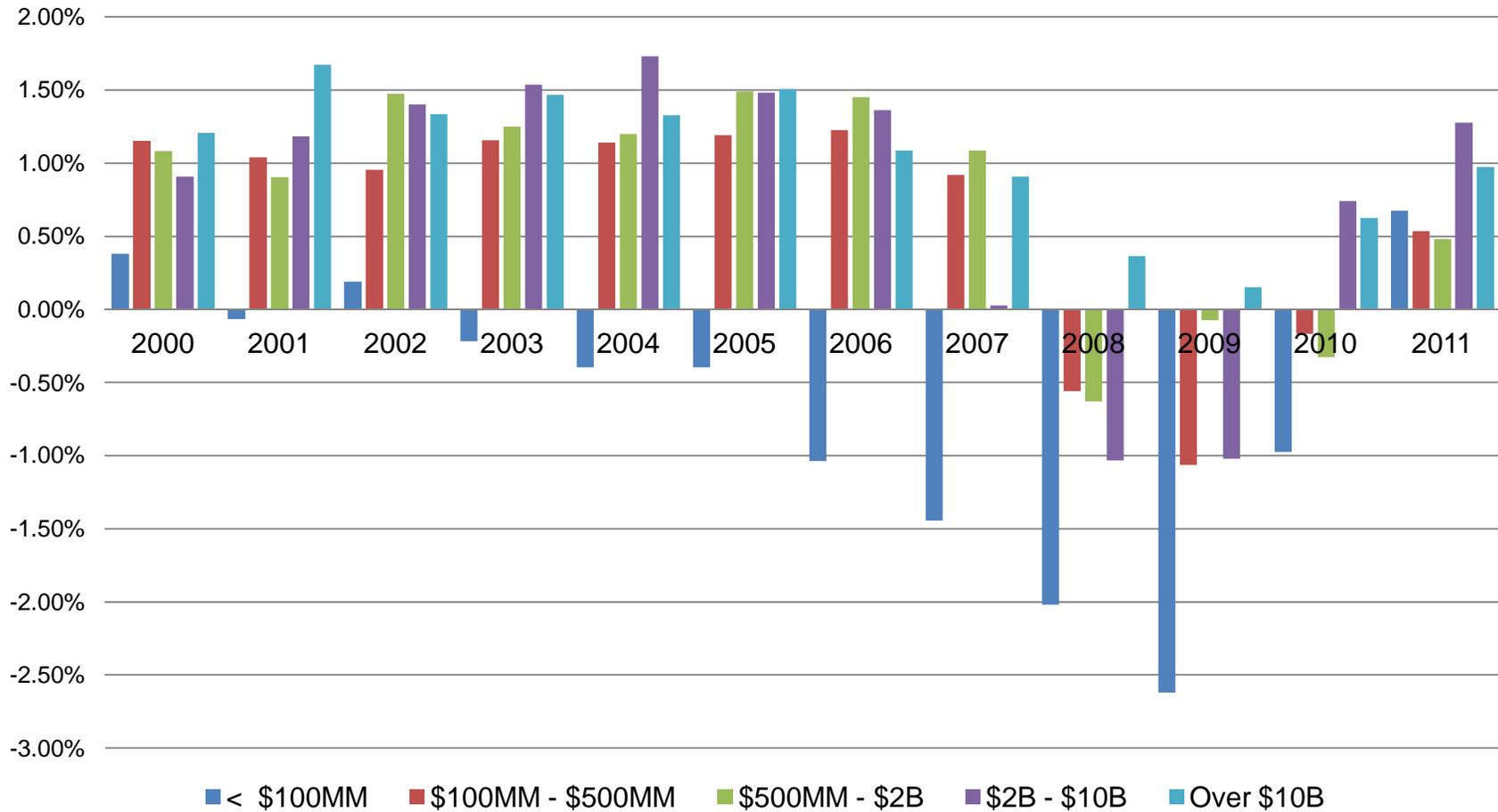


# Total Assets of California Headquartered Banks By Asset Size Group



# Return on Assets

## Annually by Asset Size Group



# Return on Assets

## California Headquartered Institutions

### Twelve-Year Arithmetic Average (2000 – 2012)

(Not static pools)

< \$100MM	-0.66%
\$100MM - \$500MM	0.63%
\$500MM - \$2B	0.78%
\$2B - \$10B	0.80%
Over \$10B	1.05%

# All State Chartered Banks

## Average Performance of Top & Bottom Quintiles

### Full Year of 2011

	Top 20%	Bottom 20%	Industry Average
Return on Assets	2.3	-1.5	0.9
Pre-Tax, Pre-Provision Return on Assets	2.8	-2.3	1.8
Net Interest Margin	5.4	2.7	3.6
Noncurrent Loans / Total Loans	7.8	0.2	2.4
Reserves for Loans / Noncurrent Loans	∞	36.0	82.6
Commercial RE Loans / Tier 1 Capital	563.9	158.2	268.1
Equity Capital / Total Assets	20.9	8.5	13.3
Loans & Leases / Assets	81.3	44.5	66.0
Crystal Ratio	60.3	2.4	16.6

# State Chartered Banks with Assets > \$2 Billion

## Average Performance of Top & Bottom Quintiles

Full Year of 2011

	Top 20%	Bottom 20%	Industry Average
Return on Assets	1.7	-0.2	1.0
Pre-Tax, Pre-Provision Return on Assets	2.6	1.0	1.9
Net Interest Margin	4.6	2.6	3.5
Noncurrent Loans / Total Loans	4.9	1.0	2.2
Reserves for Loans / Noncurrent Loans	205.1	39.0	83.3
Commercial RE Loans / Tier 1 Capital	485.0	144.0	247.6
Equity Capital / Total Assets	17.6	9.0	13.4
Loans & Leases / Assets	79.0	45.4	66.7
Crystal Ratio	32.0	6.4	15.1

State Chartered Banks with Assets between \$500MM to \$2 Billion  
Average Performance of Top & Bottom Quintiles  
Full Year of 2011

	Top 20%	Bottom 20%	Industry Average
Return on Assets	1.4	-0.5	0.7
Pre-Tax, Pre-Provision Return on Assets	2.4	0.3	1.4
Net Interest Margin	4.6	2.6	3.6
Noncurrent Loans / Total Loans	7.4	0.6	2.9
Reserves for Loans / Noncurrent Loans	430.9	41.4	85.4
Commercial RE Loans / Tier 1 Capital	595.0	162.6	304.1
Equity Capital / Total Assets	16.4	8.4	12.3
Loans & Leases / Assets	76.8	44.1	61.3
Crystal Ratio	54.7	4.7	20.7

State Chartered Banks with Assets between \$100 to \$500MM  
Average Performance of Top & Bottom Quintiles  
Full Year of 2011

	Top 20%	Bottom 20%	Industry Average
Return on Assets	1.9	-1.1	0.8
Pre-Tax, Pre-Provision Return on Assets	2.9	-0.1	1.6
Net Interest Margin	5.2	2.9	3.8
Noncurrent Loans / Total Loans	8.5	0.1	3.2
Reserves for Loans / Noncurrent Loans	∞	33.2	73.3
Commercial RE Loans / Tier 1 Capital	565.9	186.0	355.3
Equity Capital / Total Assets	18.8	9.1	13.7
Loans & Leases / Assets	81.8	49.9	67.4
Crystal Ratio	64.9	2.3	22.7

# State Chartered Banks with Assets < \$100MM

## Average Performance of Top & Bottom Quintiles

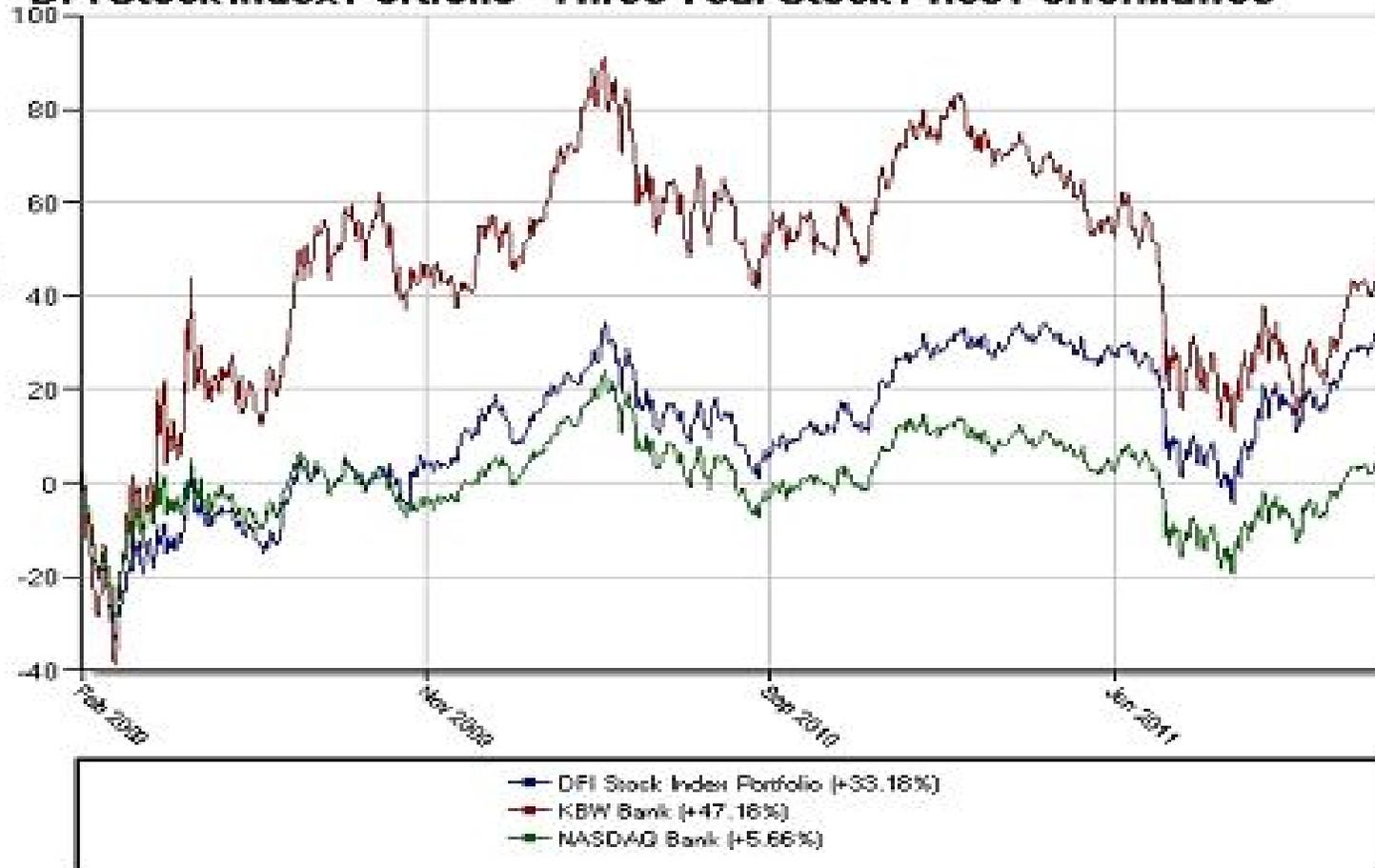
Full Year of 2011

	Top 20%	Bottom 20%	Industry Average
Return on Assets	1.7	-2.1	0.6
Pre-Tax, Pre-Provision Return on Assets	1.2	-1.8	-1.3
Net Interest Margin	5.8	3.7	5.7
Noncurrent Loans / Total Loans	5.1	0.4	2.7
Reserves for Loans / Noncurrent Loans	1,945.7	70.8	113.3
Commercial RE Loans / Tier 1 Capital	383.3	171.2	265.0
Equity Capital / Total Assets	20.3	8.5	15.4
Loans & Leases / Assets	80.7	56.2	69.7
Crystal Ratio	45.8	2.2	20.4

**State Chartered Banks**  
Average Performance of Top & Bottom Quintiles  
Full Year of 2011

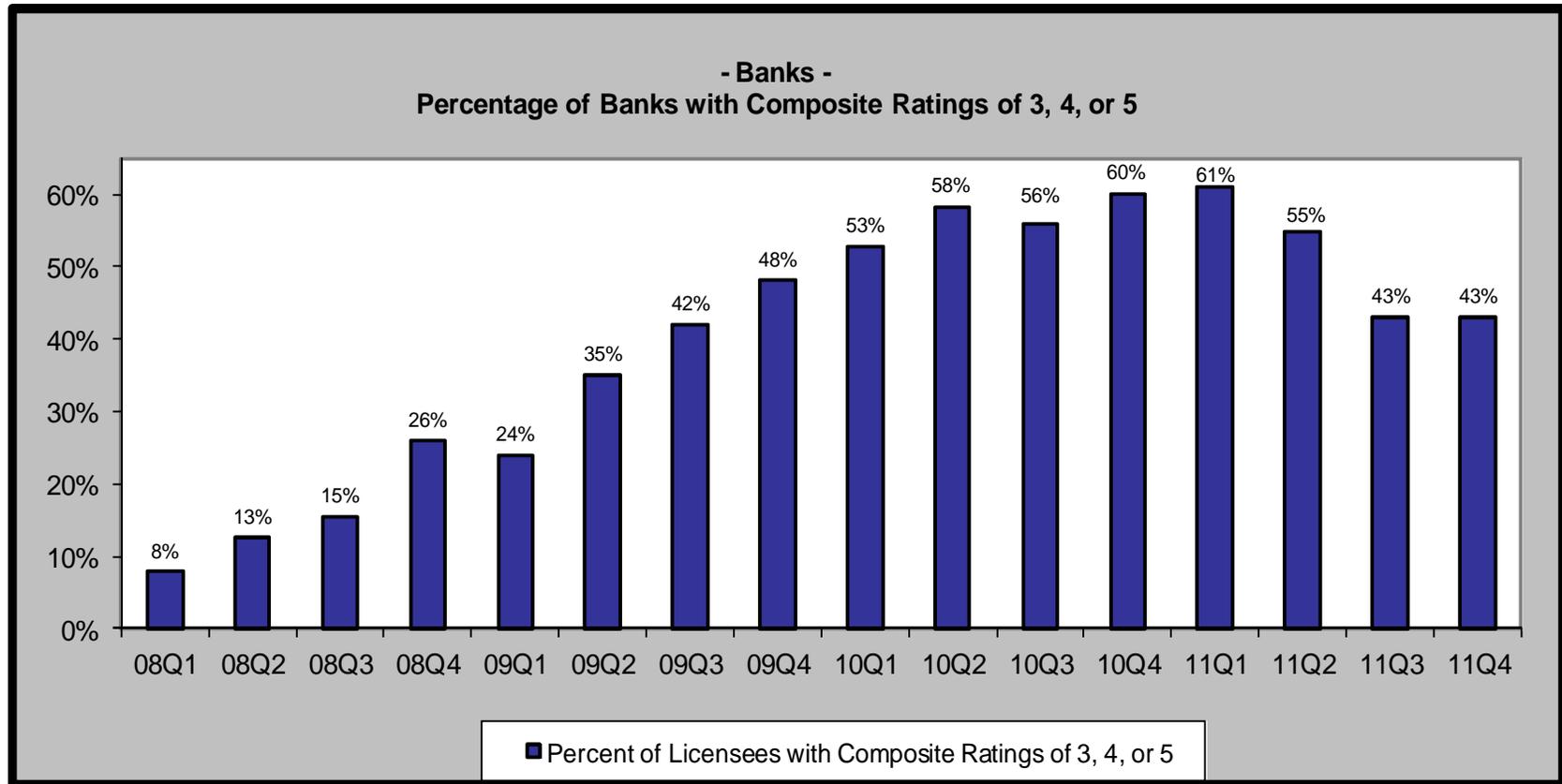
Asset Size	< \$100MM			\$100 to \$500MM			\$500MM to \$2 Billion			> \$2 Billion			All Banks		
	Top 20%	Bottom 20%	Average	Top 20%	Bottom 20%	Average	Top 20%	Bottom 20%	Average	Top 20%	Bottom 20%	Average	Top 20%	Bottom 20%	Average
Return on Assets	1.7	-2.1	0.6	1.9	-1.1	0.8	1.4	-0.5	0.7	1.7	-0.2	1.0	2.3	-1.5	0.9
Pre-Tax, Pre-Provision Return on Assets	1.2	-1.8	-1.3	2.9	-0.1	1.6	2.4	0.3	1.4	2.6	1.0	1.9	2.8	-2.3	1.8
Net Interest Margin	5.8	3.7	5.7	5.2	2.9	3.8	4.6	2.6	3.6	4.6	2.6	3.5	5.4	2.7	3.6
Noncurrent Loans / Total Loans	5.1	0.4	2.7	8.5	0.1	3.2	7.4	0.6	2.9	4.9	1.0	2.2	7.8	0.2	2.4
Reserves for Loans / Noncurrent Loans	1,945.7	70.8	113.3	∞	33.2	73.3	430.9	41.4	85.4	205.1	39.0	83.3	∞	36.0	82.6
Commercial RE Loans / Tier 1 Capital	383.3	171.2	265.0	565.9	186.0	355.3	595.0	162.6	304.1	485.0	144.0	247.6	563.9	158.2	268.1
Equity Capital / Total Assets	20.3	8.5	15.4	18.8	9.1	13.7	16.4	8.4	12.3	17.6	9.0	13.4	20.9	8.5	13.3
Loans & Leases / Assets	80.7	56.2	69.7	81.8	49.9	67.4	76.8	44.1	61.3	79.0	45.4	66.7	81.3	44.5	66.0
Crystal Ratio	45.8	2.2	20.4	64.9	2.3	22.7	54.7	4.7	20.7	32.0	6.4	15.1	60.3	2.4	16.6

### DFI Stock Index Portfolio - Three Year Stock Price Performance

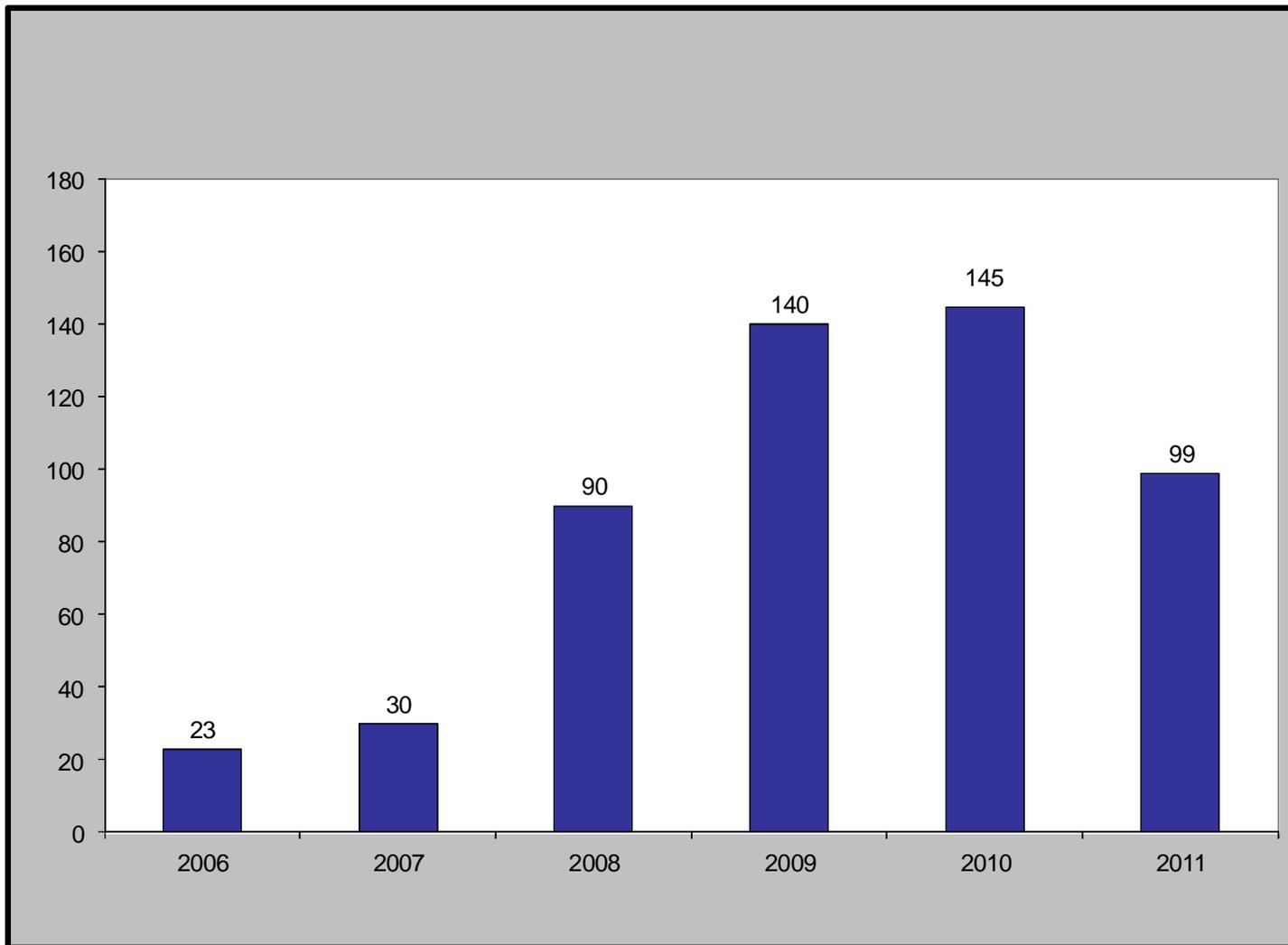


As of the close of business Fri 3 Feb 2012

# Decrease in Problem Banks



# Enforcement Actions as of January 18, 2012



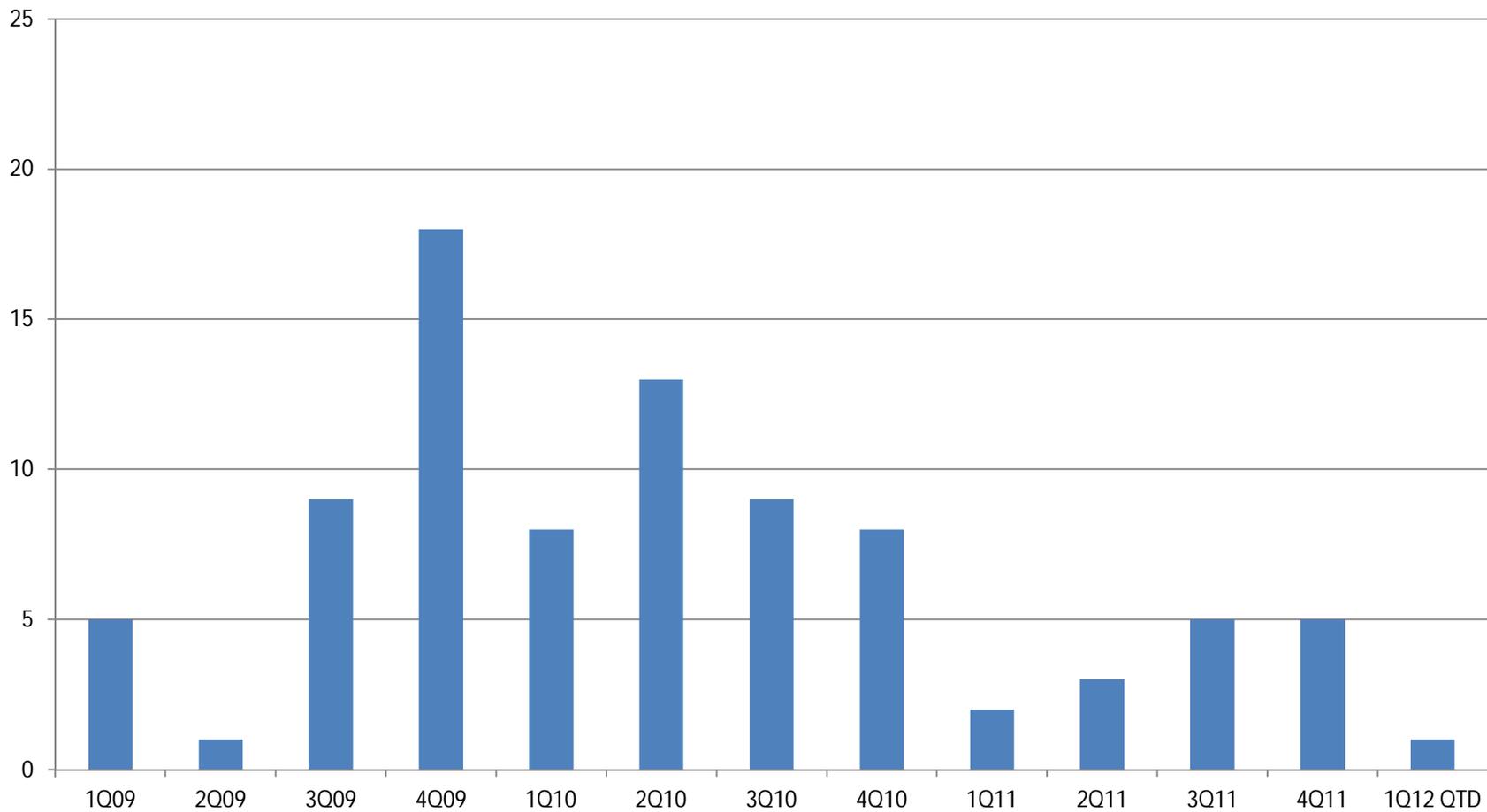
# Examination Trends as of 12/31/2011

		CURRENT RATING				
		1	2	3	4	5
PRIOR RATING	none	0	1	0	0	0
	1	1	3	0	0	0
	2	0	66	4	2	0
	3	0	34	37	8	1
	4	0	1	6	14	2
	5	0	0	0	2	4



Note: 1 institution has not yet been assigned a rating

# California Chartered Institutions Completed Capital Offerings by Quarter



# Equity Offerings by California State Chartered Banks Since 2009

- 52 state-chartered banks in California or their BHCs completed 104 equity offerings that raised \$6.9 billion.
- Number of completed offerings by CAMELS rating at the time of the offering:

<u>CAMELS</u>	<u>Rating at Offering Date</u>
1	0
2	22
3	39
4	35
5	4
<u>Unrated</u>	<u>4</u>
Total	104

# Capital Purchase Program All California Banks

Period Ending 12/31/2011 (in million \$)

<u>Type of Bank</u>	Number that <u>Accepted</u>	Total <u>Purchase</u>	Total Capital <u>Repayment</u>	Remaining <u>Investment</u>	Number of Banks <u>Remaining</u>
State Banks	53	1,948.8	867.8	763.3	25
National Banks	15	686.7	229.6	452.1	8
Federal Savings Banks	5	46.5	24.2	22.3	3
Total	73	\$2,682.0	\$1,121.5	\$1,237.7	36

# California SBLF Participants

## (In Thousands of Dollars)

Bank Type	Number of Participants	Outstanding SBLF Funding	Qualified Small Business Lending as of 9/30/11		
			Baseline Level	Current Level	Increase (Decrease) over Baseline
State	22	214,144	2,090,477	2,322,793	232,316
National	1	12,600	139,556	115,216	(24,340)
FSB	1	32,000	36,082	34,320	(1,762)
<b>Total</b>	<b>24</b>	<b>\$258,744</b>	<b>\$2,266,115</b>	<b>\$2,472,329</b>	<b>\$206,214</b>

# California Bank and Thrift Failures 2009 – Present

	State		OCC/OTS		Total	
	#	\$	#	\$	#	\$
2009	11	23,755,797	6	21,608,606	17	45,364,403
2010	9	4,626,697	3	4,650,500	12	9,277,197
2011	2	409,598	2	543,455	4	953,053
Total	22	28,792,092	11	26,802,561	33	55,594,653

\* Total assets are in thousands as of quarter-end prior to failure.

# Is the Community Banking Business Model At Risk? (FIG Partners 2011)

- Challenging revenue environment largely, but not entirely cyclical
  - California Banking in the 1930s
  - Interchange and overdraft fee restrictions not helping
- How will community banks generate a reasonable ROI?
- What is the real lesson of the crisis for community bank supervision?
- Indirect impact of regulation & supervision of large banks and other “SIFIs”

# Is the Community Banking Business Model At Risk? (FIG Partners 2012)

- Banks of all sizes facing significant headwinds that are expected to persist (more on this)
- Question remains: How will community banks generate a reasonable ROI?
- Community banks enjoy strong popular and political support
- Favorable indirect impact of regulation & supervision of large banks and other "SIFIs"
- Post crisis regulatory expectations are higher, but desire on the part of regulatory leadership to be appropriately supportive of community banking

# Community Banking Headwinds & Challenges

- Slow economy, risk aversion, continuing deleveraging process => sluggish loan growth environment
- Most CA markets are highly competitive => loan pricing and terms favorable to borrowers on a risk-adjusted basis
- Real estate collateral values depressed in many markets
- Low interest rates/flat yield curve driving down NIM. Are they contributing to a liquidity trap?
- High cost of equity capital for smaller banks => dilutive deals
- M&A hurdles (governance, accounting, pricing differences)
- Identifying the next generation of leadership

# Comments on the Interest Rate Environment

- “With retail accounts stripped of most of their earnings potential – the risk-free spread between the average cost of deposits and two-year treasuries fell to nothing today from 2.3% in 2006 – the simplest and safest form of bank income has shriveled up...the strain of the current environment can lure banks into fields in which they have no natural advantage.” *American Banker* December, 14, 2011
- “What incentive does a US bank have to extend maturity to a two or three-year term when Treasury rates at that level of the curve are below the 25 bps available to them overnight from the Fed?” Bill Gross, *Financial Times*, February 7, 2012

# IMF Global Growth Forecast, Jan. 2012

