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Interest builds in Small Business Lending Fund

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By Kevin Dobbs

Skeptics still loom large, but a new federal program aimed at juicing small-business lending is attracting the attention of some community bankers — their interests piqued by the prospect of cheap capital.

The new $30 billion Small Business Lending Fund, which President Barack Obama touted during his recent State of the Union address, was created for community banks — those with under $10 billion in assets — to get inexpensive capital to boost lending to small businesses. Such businesses happen to be the lifeblood for many community banks, and many of these banks also happen to be hard-pressed to find affordable capital elsewhere, so this confluence of factors is fueling interest, bankers and analysts say.

Under the program, for which the U.S. Treasury is scheduled to begin making investments during the current quarter, banks that can show substantial hikes in small-business lending — 10% or more — will have the interest they pay on the SBLF capital reduced from 5% to as little as 1%. Banks with less than $1 billion in assets can apply for amounts up to 5% of risk-weighted assets, while those with between $1 billion and $10 billion in assets could be eligible for up to 3%.

MidSouth Bancorp Inc. President and CEO Rusty Cloutier said his Lafayette, La.-based bank intends to apply for as much as $32 million from the fund. While it is putting the finishing touches on its application, he said he had received an informal OK from his regulators to do so.

"We think we can do it — put that money to work — and get that rate down to 1%," Cloutier told SNL. He said the oil industry in Louisiana is gaining momentum as prices at the pump have increased in recent months. "We're starting to see things pick up, and we expect there to be more demand from the oil field service industry."

Cloutier estimated MidSouth will need to lend out $40 million to $45 million over the next two years to bring its rate on the government money down to 1%.

"This is an inexpensive way to get capital, put it to work and grow a little," Cloutier said. "And if we're wrong, and demand doesn't pick up, then we just give the government its money back."

Cloutier said his bank could tap the markets, but he would rather not risk diluting shareholders. Moreover, he said, many other smaller community banks, those under approximately $500 million in assets, are virtually being shut out of the capital markets. "So I think you'll see a lot of them look into this," Cloutier said.

The Treasury is not releasing the names of applicants as they come in, so it is not known precisely how many have applied so far, but at least 18 banks and thrifts have publicly expressed interest, according to SNL research. The Independent Community Bankers of America, which expects that several dozen banks will apply for funding from the small-business program, has estimated that the $30 billion fund could translate into as much as $300 billion in new credit to local small businesses.

Fort Washington, Penn.-based Vantage Point Bank is among those to announce that it has applied to use the Small Business Lending Fund. It is seeking $2.9 million. "This program gives small banks … the fuel to lend more to small businesses and help rebuild the local economy," Chairman and CEO Walter Tillman Jr. said in a statement. The program "will play a huge role in getting the economy moving forward again."

Mark Fitzgibbon, research director at Sandler O'Neill & Partners, told SNL that the rules were "late in coming out," noting that the program was outlined last year but that rules were finalized only recently, "so it's just now that banks feel they've got a real good sense how this will work," explaining why banks are coming forward early this year.

He agreed that smaller community banks are struggling to tap the markets for capital, and many of these are likely to take a look at the SBLF. Others that still hold assistance funds from the Treasury's Troubled Asset Relief Program may view the small-business lending fund as an opportunity to pay off TARP and replace that capital with a less-expensive government infusion.

But Fitzgibbon also said many are nervous about the idea, pointing out that banks collectively faced a public perception backlash with TARP, as customers often viewed such funding simply as government bailouts.

"Many banks realized that TARP wasn't a capital panacea," Fitzgibbon said, "so while this new fund looks good on paper, people are leery of getting in bed with the government."

William Dunkelberg, chairman of Marlton, N.J.-based Liberty Bell Bank, told SNL that "there may well be banks that take it in order to get rid of their TARP." But he said most others are skeptical. "We won't use it."

He said the biggest challenge for most healthy banks is not a lack of money to make loans but finding creditworthy customers who want to borrow. "It's still about demand," he said. "Until businesses are confident enough to start investing, they won't come in and borrow, whether the money they are borrowing is our money or the government's."

Cloutier said, in conversations with colleagues, he has sensed apprehension about working with the government, but he thinks in this case the trepidation is unwarranted.

"People don't want to be associated with the government, but we're an industry totally regulated by the government," Cloutier said. Regulators "are all over the place, so we're already associated with the government. So if I can get 1% capital instead of diluting my shareholders, why wouldn't I?"

Jon Winick, president of Clark Street Capital Management, started an advisory service for community banks seeking access to capital from the Small Business Lending Fund. He told SNL that, in its early stages, "a lot of banks out there are showing cautious interest" in the program.

Likely candidates include banks that still have TARP — indicating they need capital — and yet are not on the FDIC's problem list, one assurance that they are not in or nearing grave trouble.

Echoing Fitzgibbon and other observers, Winick said many small banks still struggling to shake off the aftereffects of recession, as well as some strong small banks that are seeking funding for growth, are finding that tapping the markets for capital is too costly and highly dilutive to existing shareholders.

So the small-business lending program "could definitely makes sense" for some banks, he said.

Potential roadblocks, however, lurk. The government set up the program specifically to bolster lending to small businesses. As such, authorities are sure to be looking closely at whether banks intend to actually put the capital they get under the program to work, or merely use it to boost capital levels and only modestly lift the lending they do. "If you're not really going to use it, then is it worth it?" Winick said.

Additionally, Winick said, he has heard from regulators who are concerned that it will be tough to gauge whether a bank is healthy enough to truly benefit from the program. The applicant pool could be peppered with banks that, while surviving, are merely limping along, extending their lives in hopes of finding a buyer on the open market. Regulators are likely to be hesitant to sign off on such banks using the small-business lending program, he said.

"It's hard to know what any given regulator will decide," Winick said. "Is it best to work with every bank that could benefit? Or am I just delaying the inevitable by allowing a weak bank to take part in this? Regulators won't say this publicly, but behind the scenes we've heard that the feeling is there are simply too many banks out there, and so the stated goal is to thin the field. If that is the goal, then it may not make sense to allow a lot of these banks to take part, from a regulator's view." *i*

One SNL Plaza, P.O. Box 2124, Charlottesville, VA 22902 Phone: 434.977.1600 News fax: 434.293.0407 www.snl.com