

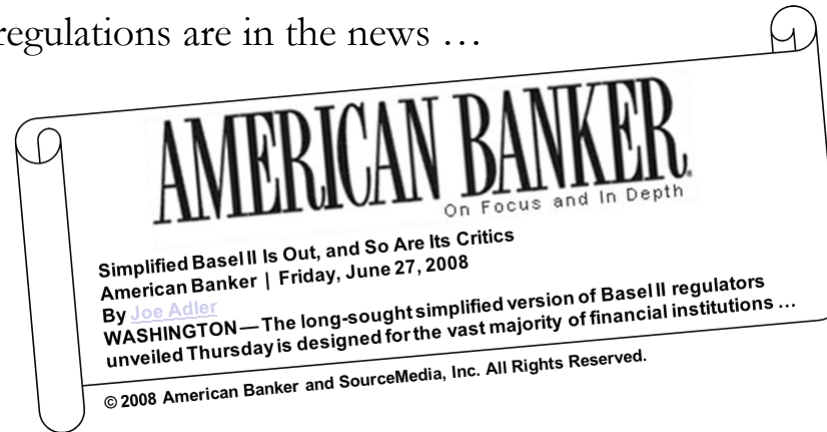
# The Impact of Standardized Basel II on Arkansas Banks

Prepared for Arkansas Bankers Association



# Executive Summary

- Basel II bank capital regulations are in the news ...

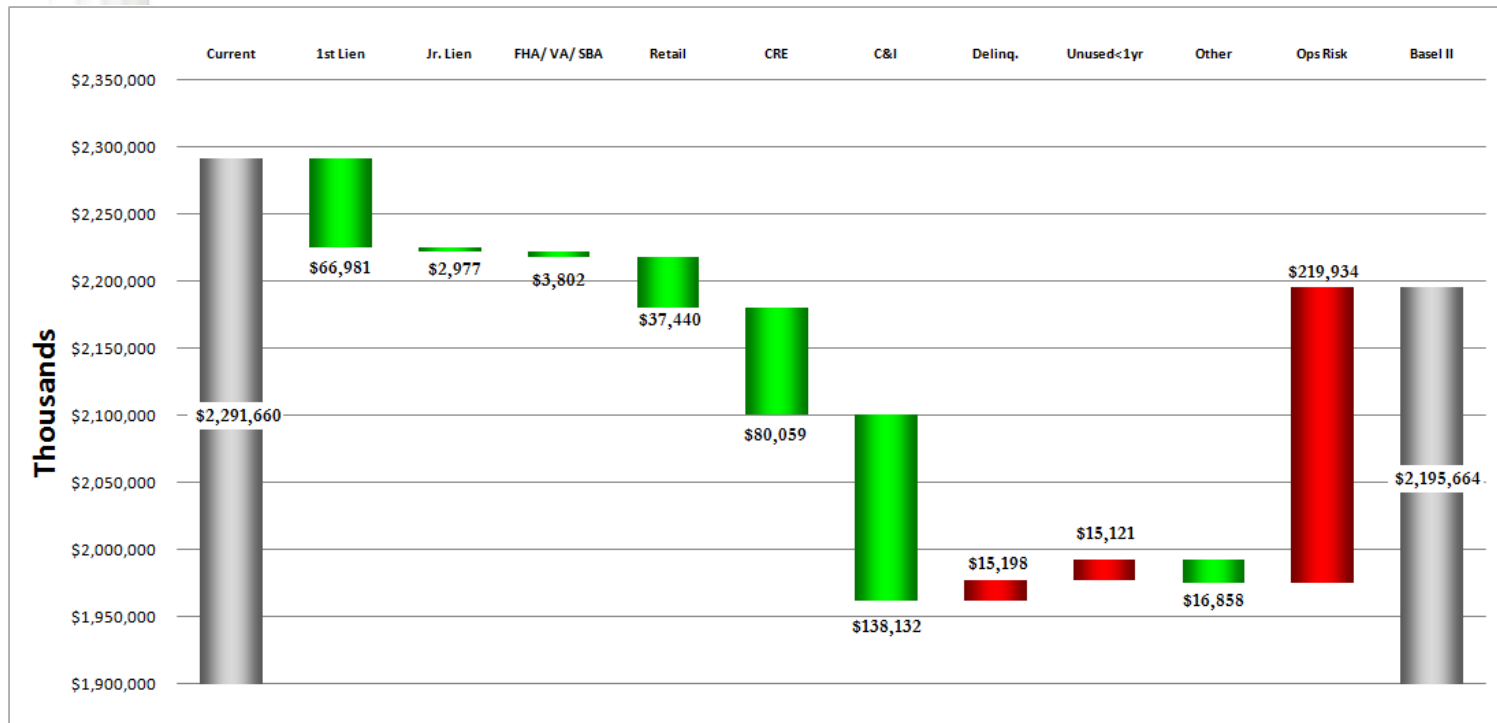


- We estimate that Standardized Basel II compliance will improve the regulatory capital ratios of 68.8% of 126 Arkansas banks and thrifts
  - Aggregate potential capital savings for all 126 banks of \$96 million
  - The median Arkansas bank would save \$0.7 million or 2.3% of their existing Tier 1 capital requirement
- Implementation is not without its challenges
  - Pillar II reporting can be complex and costly
  - Compliance requires demonstrated capital management capabilities
- Are your members aware of and prepared for these changes?
  - Second Pillar Consulting is uniquely positioned to help banks comply with Pillar II and obtain the capital relief they deserve

# Arkansas Banks can save up to \$96 million in required capital under Standardized Basel II and improve risk management

## Capital savings estimate and asset category contribution

Regulatory Capital Requirement

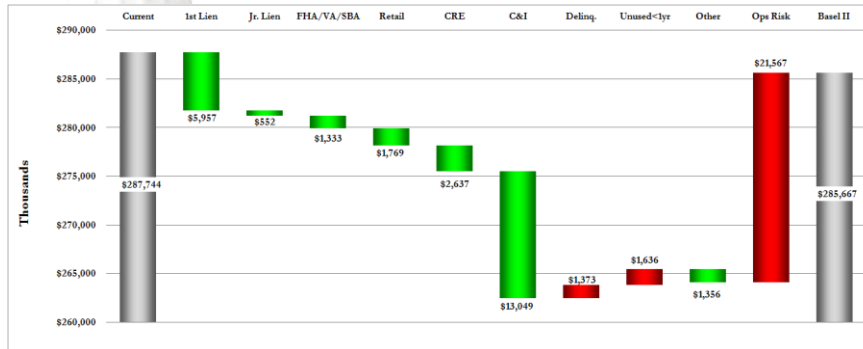


Source: 2008Q3 Call Reports; SPC estimates

# For Home BancShares, Inc., a representative Arkansas bank, Basel II regulatory capital savings can be stockpiled or deployed

Capital Savings: \$2.1 million or 0.7%

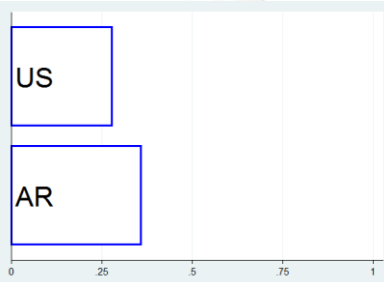
Regulatory Capital Requirement



## Home BancShares, Inc. Conway, AR Highlights

- *Stockpile.* Under Basel II, total RBC increases from 14.3% to 14.4%, an amount equal to \$2.1 million or 0.7% of the existing capital base.
- *Deploy.* Incremental capital can be deployed with a variety of balance sheet actions that preserve the current 14.3% total RBC ratio:
  - Issue a special dividend of \$0.11 per share
  - Repurchase 78,603 shares, increasing EPS \$0.00 or 0.4%
  - Organically grow assets by \$17 million

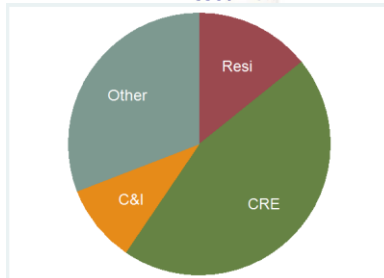
Capital Savings Percentile



Capital Metrics and Management

Total Assets (millions)	\$2,651	
Gross Income Margin	3.5%	
Tangible Common Equity	9.0%	
Leverage Ratio	11.3%	
Capital Estimates	Current	Basel II
Tier 1 RBC	13.0%	13.1%
Total RBC	14.3%	14.4%
Potential Use of Basel II Capital Savings		
Special Dividend (\$/share)	\$0.11	
Share Repurchase (7/29/2008 price)		
Number of Shares	78,603	
Change in EPS	\$0.00	
Organic Asset Growth (millions)	\$17	

Asset Mix



Upon request, Second Pillar Consulting can provide similar information for all 126 Arkansas banks free of charge

# Arkansas banks with the highest percentage changes in regulatory capital under Standardized Basel II

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Source: 2008Q3 Call Reports; SPC estimates

# Arkansas banks with the lowest or negative percentage changes in regulatory capital under Standardized Basel II

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Source: 2008Q3 Call Reports; SPC estimates

## But banks must be prepared to answer the tough risk management questions posed by Basel II compliance

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- Do you have a well-functioning risk oversight structure?
- Do you have clear risk management policies and procedures?
- Have you identified the important risks faced by your institution?
- Have you articulated an institutional appetite for risk-taking?
- Do you have accessible data on the risk characteristics of your existing portfolio?
- Do you have accessible data on the past performance of your portfolio?
- Do you have personnel that can fill critical risk assessment gaps?
- Do you actively manage and plan your capital position?
- Are you committed to enhancing your overall risk and capital management?

# Second Pillar Consulting can help banks prepare for Basel II compliance

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- Our principals have over thirty years of experience in enterprise risk management, regulatory capital compliance, and regulatory relations
  - Supported International Basel II compliance at a top-ten bank
    - Developed analytical and reporting capabilities
    - Created governance structure and supporting policies
    - Led regulatory exams for approval
  - Managed risk in retail banking, commercial banking, and insurance
  - Focused on building strong regulatory relationships
    - Active participants in several Basel II industry and regulatory forums that facilitated drafting the new rules
    - Frequent speakers at industry and regulatory conferences on Basel
    - Several Basel II academic papers written jointly with regulators

## Summary

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- Second Pillar Consulting is uniquely positioned to help banks comply with Basel II and get the capital relief they deserve
  - Services
    - Detailed Capital Savings Estimate
    - Gap Analysis
    - The Internal Capital Adequacy Assessment Process or ICAAP
  - Education
    - We conduct seminars for institutions and organizations on topics including Basel II compliance, Enterprise Risk Management, Capital Management, and Balance Sheet Strategy
  - Facilitation
    - We are currently coordinating the NPR response for the Risk Management Association and can help organizations and institutions with their response

## Contact Information

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