

# **The Impact of Standardized Basel II on California Banks**

**Prepared for California Bankers Association**



# Executive Summary

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

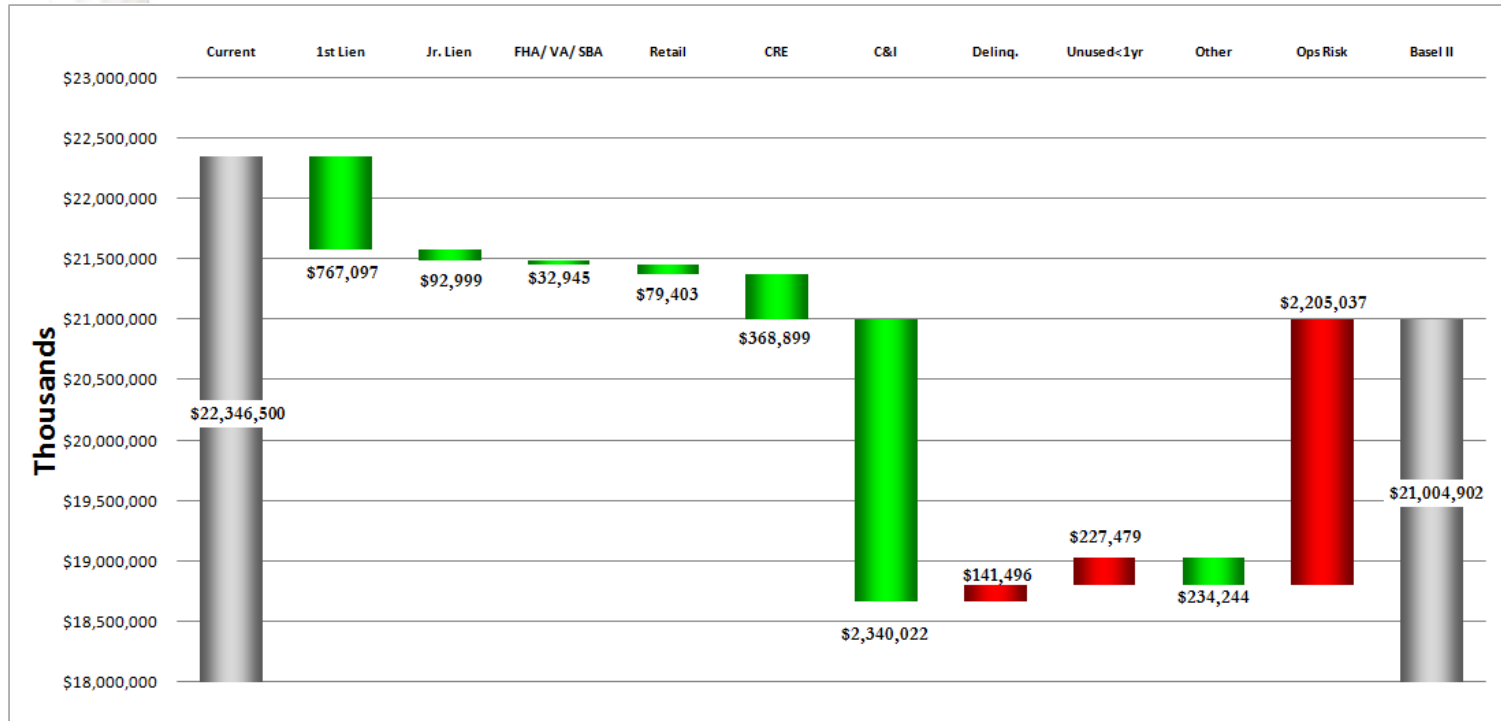


- We estimate that Standardized Basel II compliance will improve the regulatory capital ratios of 73.5% of 274 California banks and thrifts
  - Aggregate potential capital savings for all 274 banks of \$1,342 million
  - The median California bank would save \$1.5 million or 3.9% of their existing Tier 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

# California Banks can save up to \$1,342 million in required capital under Standardized Basel II and improve risk management

## Capital savings estimate and asset category contribution

Regulatory Capital Requirement

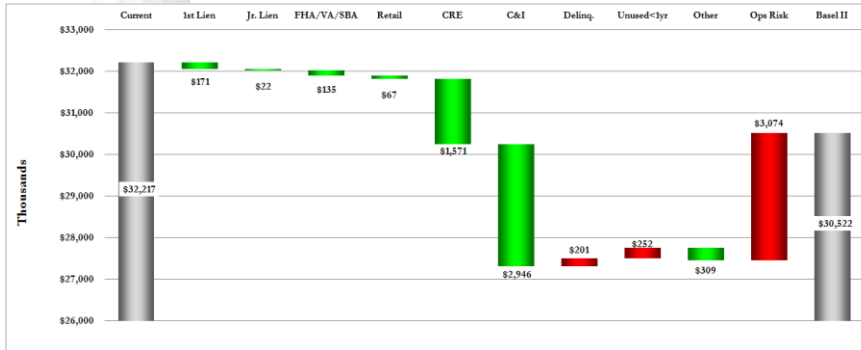


Source: 2008Q3 Call Reports; SPC estimates

# For Valley Business Bank, a representative California bank, Basel II regulatory capital savings can be stockpiled or deployed

Capital Savings: \$1.7 million or 5.1%

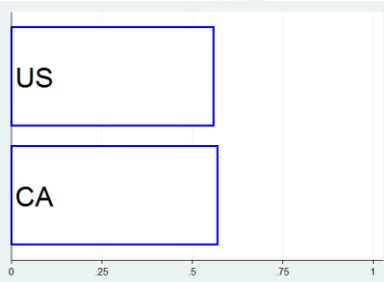
Regulatory Capital Requirement



## Valley Business Bank Visalia, CA Highlights

- *Stockpile.* Under Basel II, total RBC increases from 13.6% to 14.3%, an amount equal to \$1.7 million or 5.1% of the existing capital base.
- *Deploy.* Incremental capital can be deployed with a variety of balance sheet actions that preserve the current 13.6% total RBC ratio:
  - Issue a special dividend of \$0.67 per share
  - Repurchase 168,608 shares, increasing EPS \$0.07 or 7.0%
  - Organically grow assets by \$15 million

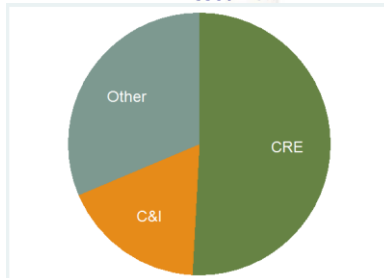
Capital Savings Percentile



Capital Metrics and Management

Total Assets (millions)	\$306	
Gross Income Margin	4.2%	
Tangible Common Equity	10.3%	
Leverage Ratio	10.5%	
Capital Estimates	Current	Basel II
Tier 1 RBC	12.5%	13.1%
Total RBC	13.6%	14.3%
Potential Use of Basel II Capital Savings		
Special Dividend (\$/share)	\$0.67	
Share Repurchase (7/29/2008 price)		
Number of Shares	168,608	
Change in EPS	\$0.07	
Organic Asset Growth (millions)	\$15	

Asset Mix



Upon request, Second Pillar Consulting can provide similar information for all 274 California banks free of charge

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

Name	City	Asset Size (\$000's)	Basel II Capital Impact	
			Dollar Change (\$000)	Percent Change
Community Valley Bank	El Centro	\$ 28,866	\$ 1,994	23.5%
California Republic Bank	Newport Beach	\$ 157,664	\$ 9,436	23.2%
Wedbush Bank	Los Angeles	\$ 26,634	\$ 3,648	23.1%
Manufacturers Bank	Los Angeles	\$ 2,107,738	\$ 49,372	20.6%
Plaza Bank	Irvine	\$ 76,644	\$ 1,130	20.5%
1st Capital Bank	Monterey	\$ 113,978	\$ 4,870	20.3%
First Vietnamese American Bank	Westminster	\$ 54,292	\$ 1,331	19.9%
Pacific Enterprise Bank	Irvine	\$ 68,376	\$ 3,763	19.7%
Security Bank of California	Riverside	\$ 237,549	\$ 5,978	18.5%
Beach Business Bank	Manhattan Beach	\$ 221,846	\$ 5,647	18.3%
Bank of Santa Clarita	Santa Clarita	\$ 134,661	\$ 3,067	17.8%
Murphy Bank	Fresno	\$ 119,502	\$ 2,447	17.4%
US Metro Bank	Garden Grove	\$ 107,880	\$ 2,581	17.4%
Private Bank of California	Los Angeles	\$ 242,349	\$ 5,377	17.3%
California Bank of Commerce	Lafayette	\$ 124,195	\$ 3,167	17.2%
CommerceWest Bank, N.A.	Irvine	\$ 235,331	\$ 5,250	16.5%
Commerce Bank of Temecula Valley	Murrieta	\$ 29,496	\$ 1,847	16.5%
Pacific Alliance Bank	Rosemead	\$ 63,581	\$ 1,879	16.0%
Bank of Napa, N.A.	Napa	\$ 60,786	\$ 2,389	15.9%
San Diego Private Bank	La Jolla	\$ 101,369	\$ 1,511	15.8%
<b>Averages</b>		<b>\$ 215,636.85</b>	<b>\$ 5,834.20</b>	<b>18.8%</b>

Source: 2008Q3 Call Reports; SPC estimates

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

Name	City	Asset Size (\$000's)	Basel II Capital Impact	
			Dollar Change (\$000)	Percent Change
1st Centennial Bancorp	Redlands	\$ 939,168	\$ (1,926)	-4.0%
RCB Corporation	Sacramento	\$ 852,495	\$ (4,245)	-4.1%
Exchange Bank	Santa Rosa	\$ 1,666,259	\$ (6,758)	-4.3%
First Regional Bancorp	Century City	\$ 2,416,060	\$ (14,009)	-4.6%
Monterey County Bank	Monterey	\$ 272,888	\$ (1,429)	-5.2%
Community Valley Bancorp	Chico	\$ 602,981	\$ (3,092)	-5.3%
Pacific Capital Bancorp	Santa Barbara	\$ 7,687,048	\$ (41,700)	-5.3%
Imperial Capital Bancorp, Inc.	La Jolla	\$ 4,116,583	\$ (23,078)	-6.2%
First Credit Bank	Los Angeles	\$ 361,687	\$ (7,298)	-6.8%
Temecula Valley Bancorp Inc.	Temecula	\$ 1,513,972	\$ (13,937)	-7.3%
Affinity Bank Holdings, Inc.	Ventura	\$ 1,249,503	\$ (7,787)	-7.4%
Farmers & Merchants Bank of Long Beach	Long Beach	\$ 3,578,193	\$ (47,620)	-7.6%
Finance & Thrift Company	Porterville	\$ 114,181	\$ (2,355)	-8.5%
Beverly Hills Bancorp Inc.	Calabasas	\$ 1,302,610	\$ (15,008)	-8.7%
Palm Desert National Bank	Palm Desert	\$ 403,019	\$ (4,298)	-9.2%
Delta Bank, National Association	Manteca	\$ 159,922	\$ (2,094)	-9.3%
Gold Country Bank, National Association	Marysville	\$ 97,387	\$ (1,256)	-10.2%
First American Trust FSB	Santa Ana	\$ 1,109,452	\$ (12,074)	-12.8%
Merchants Bank of California, National Ass	Carson	\$ 80,670	\$ (2,531)	-15.5%
Gateway Business Bank	Cerritos	\$ 194,956	\$ (10,272)	-23.4%
<b>Averages</b>		<b>\$ 1,435,952</b>	<b>\$ (11,138)</b>	<b>-8.3%</b>

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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