

The Impact of Standardized Basel II on Maryland Banks

Prepared for Maryland Bankers Association



Executive Summary

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

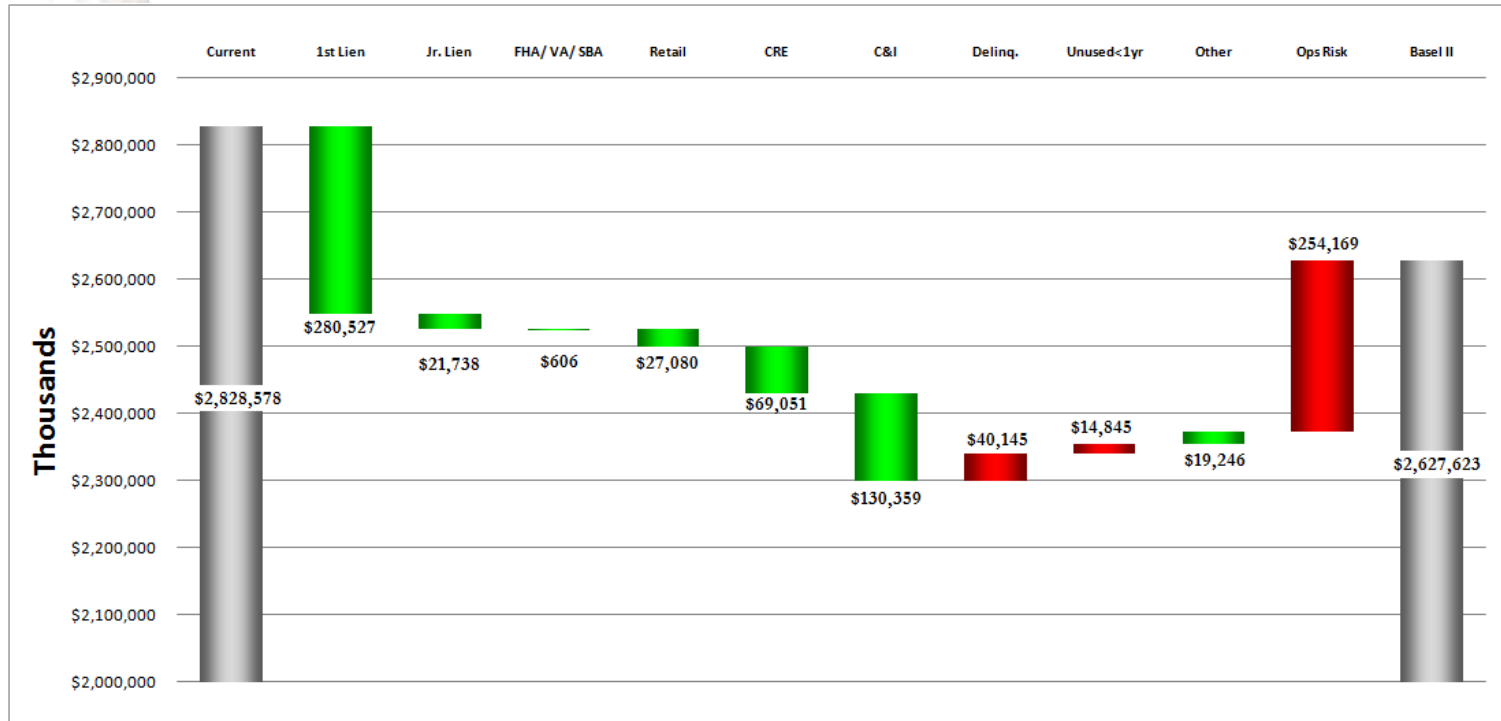


- We estimate that Standardized Basel II compliance will improve the regulatory capital ratios of 77.2% of 92 Maryland banks and thrifts
 - Aggregate potential capital savings for all 92 banks of \$201 million
 - The median Maryland bank would save \$1.6 million or 7.1% of their existing Tier 1 capital 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

Maryland Banks can save up to \$201 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 Bank of Glen Burnie, a representative Maryland bank, Basel II regulatory capital savings can be stockpiled or deployed

Capital Savings: \$2.5 million or 7.9%

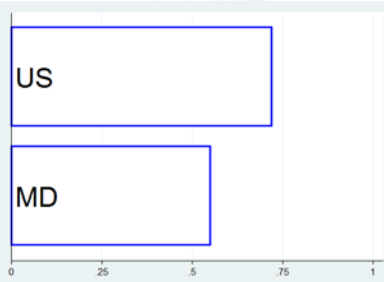
Regulatory Capital Requirement



Bank of Glen Burnie Glen Burnie, MD Highlights

- *Stockpile.* Under Basel II, total RBC increases from 14.9% to 16.1%, an amount equal to \$2.5 million or 7.9% of the existing capital base.
- *Deploy.* Incremental capital can be deployed with a variety of balance sheet actions that preserve the current 14.9% total RBC ratio:
 - Issue a special dividend of \$0.85 per share
 - Repurchase 282,743 shares, increasing EPS \$0.10 or 10.5%
 - Organically grow assets by \$24 million

Capital Savings Percentile



Capital Metrics and Management

Total Assets (millions)	\$330	
Gross Income Margin	4.4%	
Tangible Common Equity	9.6%	
Leverage Ratio	10.3%	
Capital Estimates	Current	Basel II
Tier 1 RBC	14.2%	15.3%
Total RBC	14.9%	16.1%
Potential Use of Basel II Capital Savings		
Special Dividend (\$/share)	\$0.85	
Share Repurchase (7/29/2008 price)		
Number of Shares	282,743	
Change in EPS	\$0.10	
Organic Asset Growth (millions)	\$24	

Asset Mix



Upon request, Second Pillar Consulting can provide similar information for all 92 Maryland banks free of charge

Maryland 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
CommerceFirst Bank	Annapolis	\$ 163,938	\$ 3,403	22.4%
T. Rowe Price Savings Bank	Baltimore	\$ 144,586	\$ 2,246	18.3%
Glen Burnie Mutual Savings Bank	Glen Burnie	\$ 64,498	\$ 983	17.7%
Howard Bank	Ellicott City	\$ 225,617	\$ 3,722	17.6%
Congressional Bank	Bethesda	\$ 174,223	\$ 3,523	17.5%
Bank of the Eastern Shore	Cambridge	\$ 227,551	\$ 3,577	16.5%
Fraternity Federal Savings & Loan Association	Baltimore	\$ 171,325	\$ 2,180	14.8%
Homewood Federal Savings Bank	Baltimore	\$ 70,741	\$ 1,209	14.6%
HarVest Bank of Maryland	Rockville	\$ 214,955	\$ 2,025	14.3%
Fairmount Federal Savings Bank	Baltimore	\$ 55,512	\$ 771	13.7%
Colombo Bank	Rockville	\$ 168,116	\$ 1,566	13.7%
Slavie Federal Savings Bank (MHC)	Bel Air	\$ 177,090	\$ 2,133	13.2%
OBA Bank	Germantown	\$ 349,780	\$ 4,658	13.1%
Provident State Bank	Preston	\$ 245,252	\$ 2,178	12.6%
Monument Bank	Bethesda	\$ 176,495	\$ 1,862	11.9%
Hull Federal Savings Bank	Baltimore	\$ 21,060	\$ 275	11.8%
Patapsco Bank	Dundalk	\$ 260,898	\$ 2,250	11.5%
Hamilton Federal Bank	Baltimore	\$ 222,576	\$ 3,277	11.2%
Damascus Community Bank	Damascus	\$ 175,918	\$ 2,003	10.8%
Arundel Federal Savings Bank	Baltimore	\$ 430,235	\$ 4,445	10.2%
Averages		\$ 187,018.30	\$ 2,414.29	14.4%

Source: 2008Q3 Call Reports; SPC estimates

Maryland 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
CommerceFirst Bank	Annapolis	\$ 163,938	\$ 3,403	22.4%
T. Rowe Price Savings Bank	Baltimore	\$ 144,586	\$ 2,246	18.3%
Glen Burnie Mutual Savings Bank	Glen Burnie	\$ 64,498	\$ 983	17.7%
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But banks must be prepared to answer the tough risk management questions posed by Basel II compliance

- 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

- 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

- 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

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