

The Impact of Standardized Basel II on Massachusetts Banks

Prepared for Massachusetts Bankers Association



Executive Summary

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

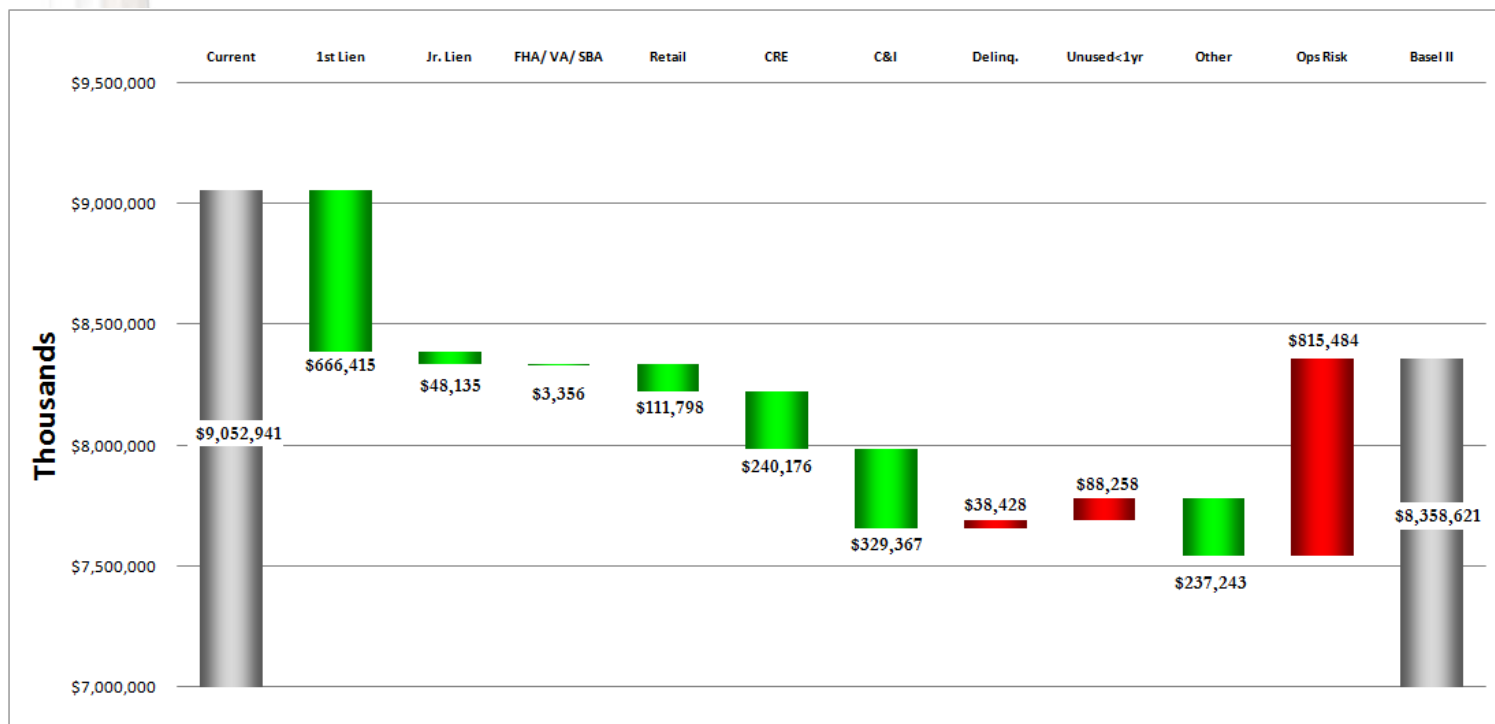


- We estimate that Standardized Basel II compliance will improve the regulatory capital ratios of 92.4% of 172 Massachusetts banks and thrifts
 - Aggregate potential capital savings for all 172 banks of \$694 million
 - The median Massachusetts bank would save \$2.4 million or 7.4% of their existing 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

Massachusetts Banks can save up to \$694 million in required capital under Standardized Basel II and improve risk management

Capital savings estimate and asset category contribution

Regulatory Capital Requirement

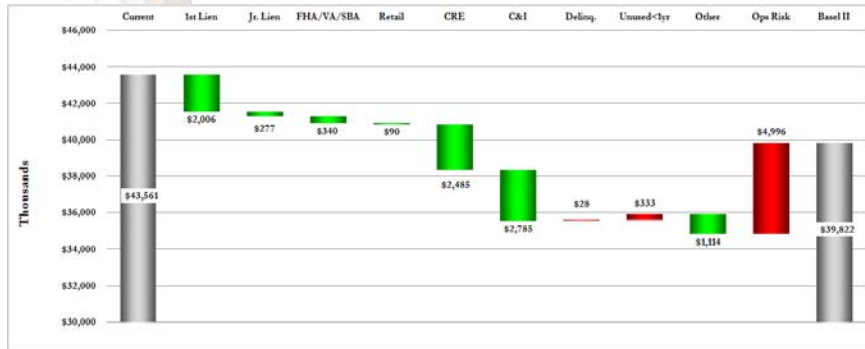


Source: 2008Q3 Call Reports; SPC estimates

For Beverly National Bank, a representative Massachusetts bank, Basel II regulatory capital savings can be stockpiled or deployed

Capital Savings: \$3.7 million or 8.5%

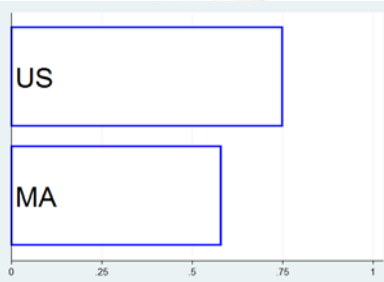
Regulatory Capital Requirement



Beverly National Bank Beverly, MA Highlights

- *Stockpile.* Under Basel II, total RBC increases from 13.4% to 14.5%, an amount equal to \$3.7 million or 8.5% of the existing capital base.
- *Deploy.* Incremental capital can be deployed with a variety of balance sheet actions that preserve the current 13.4% total RBC ratio:
 - Issue a special dividend of \$1.42 per share
 - Repurchase 239,657 shares, increasing EPS \$0.12 or 9.6%
 - Organically grow assets by \$38 million

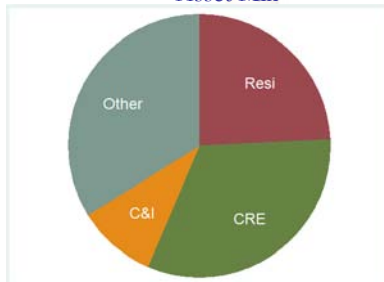
Capital Savings Percentile



Capital Metrics and Management

Total Assets (millions)	\$483	
Gross Income Margin	4.3%	
Tangible Common Equity	8.2%	
Leverage Ratio	9.0%	
Capital Estimates	Current	Basel II
Tier 1 RBC	12.2%	13.3%
Total RBC	13.4%	14.5%
Potential Use of Basel II Capital Savings		
Special Dividend (\$/share)	\$1.42	
Share Repurchase (7/29/2008 price)	239,657	
Change in EPS	\$0.12	
Organic Asset Growth (millions)	\$38	

Asset Mix



Upon request, Second Pillar Consulting can provide similar information for all 172 Massachusetts banks free of charge

Massachusetts 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
Nuvo Bank & Trust Company	Springfield	\$ 12,330	\$ 1,978	24.7%
Patriot Community Bank	Woburn	\$ 55,937	\$ 1,698	23.2%
Bank of Cape Cod	Hyannis	\$ 72,613	\$ 1,866	21.2%
Coastal Affiliates, MHC	Yarmouth Port	\$ 593,756	\$ 8,773	20.9%
Hyde Park Savings Bank	Boston	\$ 981,687	\$ 19,101	20.8%
North Cambridge Co-operative Bank	Cambridge	\$ 86,215	\$ 2,752	18.8%
Institution for Savings in Newburyport and	Newburyport	\$ 953,016	\$ 21,481	18.5%
Millbury Savings Bank	Millbury	\$ 193,680	\$ 2,918	17.1%
Pentucket Bank	Haverhill	\$ 500,312	\$ 8,169	16.0%
South Shore Co-operative Bank	Weymouth	\$ 195,196	\$ 2,106	15.1%
Washington Savings Bank	Lowell	\$ 162,921	\$ 2,077	15.1%
Belmont Savings Bank	Belmont	\$ 481,957	\$ 5,581	15.1%
Marlborough Savings Bank	Marlborough	\$ 347,743	\$ 4,826	15.1%
Narragansett Financial Corp	Fall River	\$ 646,912	\$ 7,697	15.0%
Foxboro Federal Savings	Foxboro	\$ 123,609	\$ 2,422	14.8%
Martha's Vineyard Savings Bank	Edgartown	\$ 470,181	\$ 6,272	14.1%
Lee Bank	Lee	\$ 295,388	\$ 3,088	13.8%
UFS Bancorp	Whitinsville	\$ 747,525	\$ 9,160	13.8%
Equitable Co-operative Bank	Lynn	\$ 99,526	\$ 1,172	13.6%
Eagle Bank	Everett	\$ 437,894	\$ 6,369	13.6%
Averages		\$ 372,919.90	\$ 5,975.25	17.0%

Source: 2008Q3 Call Reports; SPC estimates

Massachusetts 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
Stoneham Savings Bank	Stoneham	\$ 451,159	\$ 936	2.5%
Central Bancorp, Inc.	Somerville	\$ 541,752	\$ 932	2.4%
Milford National Bank and Trust Company	Milford	\$ 323,431	\$ 449	1.9%
Mayflower Co-operative Bank	Middleboro	\$ 239,438	\$ 340	1.7%
Framingham Co-operative Bank	Framingham	\$ 345,013	\$ 805	1.1%
Chelsea Provident Co-operative Bank	Chelsea	\$ 45,315	\$ 48	1.0%
Bank of Fall River, A Co-Operative Bank	Fall River	\$ 133,134	\$ 108	0.8%
Lowell Five Cents Savings Bank	Lowell	\$ 661,666	\$ 779	0.8%
Commerce Bancshares Corp.	Worcester	\$ 1,078,063	\$ 902	0.7%
Middlesex Federal Savings, F.A.	Somerville	\$ 379,958	\$ 344	0.7%
Century Bancorp, Inc.	Medford	\$ 1,745,250	\$ 369	0.2%
East Bridgewater Savings Bank	East Bridgewater	\$ 135,884	\$ (28)	-0.2%
Winter Hill Bank, FSB	Somerville	\$ 245,721	\$ (109)	-0.4%
Norwood Co-operative Bank	Norwood	\$ 431,575	\$ (1,323)	-2.1%
Boston Private Financial Holdings, Inc.	Boston	\$ 7,068,239	\$ (18,987)	-2.8%
First Federal Savings Bank of Boston	Boston	\$ 60,945	\$ (515)	-4.6%
Fidelity Personal Trust Company, FSB	Boston	\$ 24,066	\$ (1,179)	-5.0%
OneUnited Bank	Boston	\$ 625,311	\$ (941)	-6.0%
Butler Bank--A Co-operative Bank (MHC)	Lowell	\$ 255,206	\$ (1,433)	-6.3%
Cambridge Bancorp	Cambridge	\$ 896,628	\$ (5,634)	-6.9%
Averages		\$ 784,388	\$ (1,207)	-1.0%

Source: 2008Q3 Call Reports; SPC estimates

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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