

The Impact of Standardized Basel II on West Virginia Banks

Prepared for West Virginia Bankers Association



Executive Summary

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

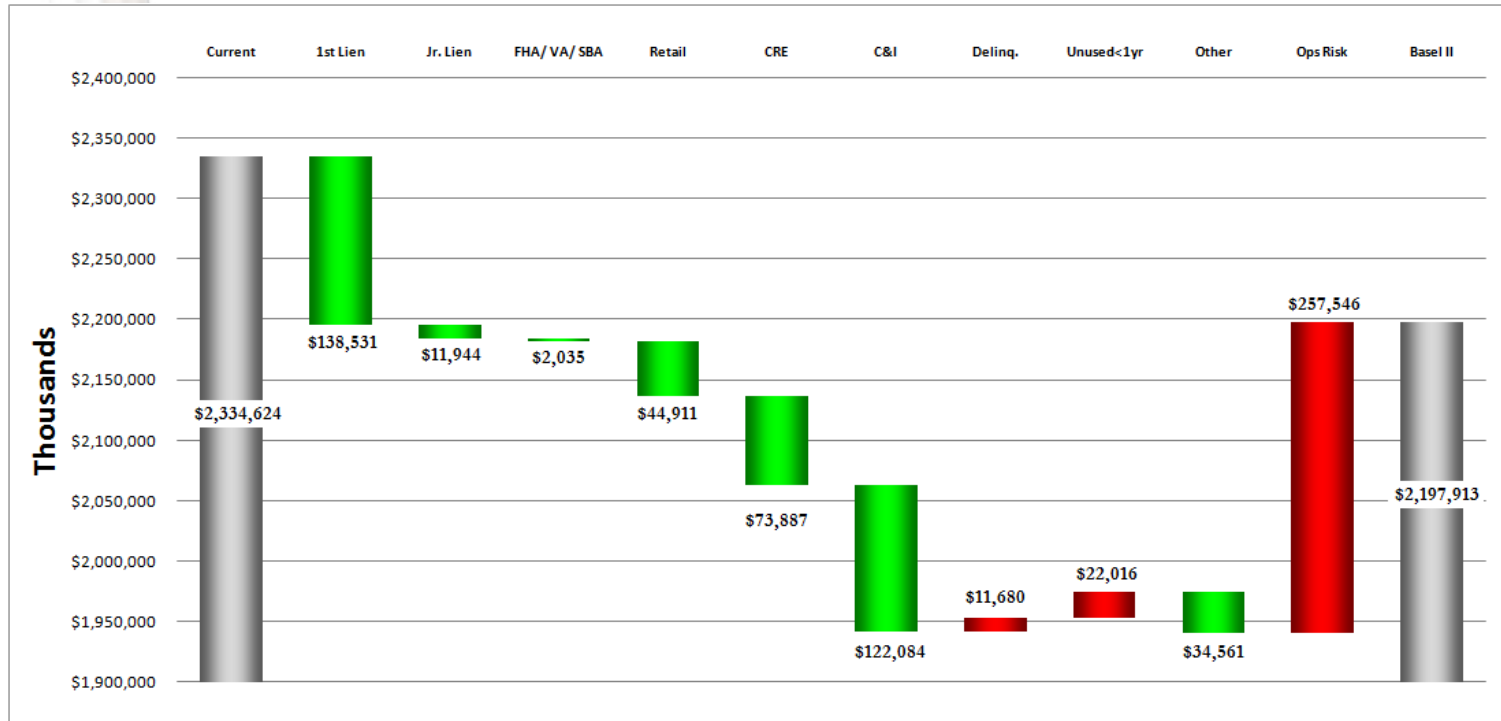


- We estimate that Standardized Basel II compliance will improve the regulatory capital ratios of 85.7% of 63 West Virginia banks and thrifts
 - Aggregate potential capital savings for all 63 banks of \$137 million
 - The median West Virginia bank would save \$1.3 million or 5.6% of their existing Tier 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

West Virginia Banks can save up to \$137 million in required capital under Standardized Basel II and improve risk management

Capital savings estimate and asset category contribution

Regulatory Capital Requirement

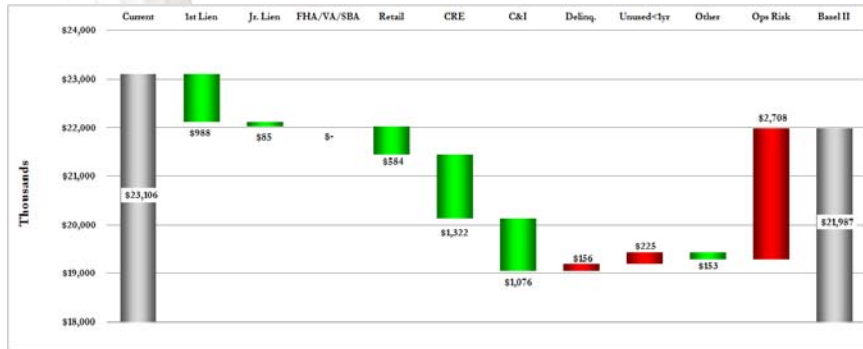


Source: 2008Q3 Call Reports; SPC estimates

For First National Bank, a representative West Virginia bank, Basel II regulatory capital savings can be stockpiled or deployed

Capital Savings: \$1.1 million or 4.6%

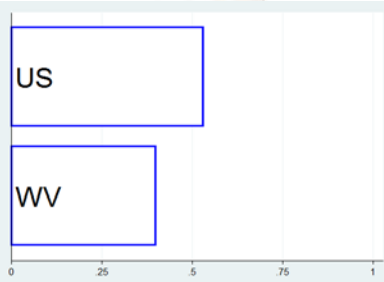
Regulatory Capital Requirement



First National Bank Ronceverte, WV Highlights

- *Stockpile.* Under Basel II, total RBC increases from 14.6% to 15.2%, an amount equal to \$1.1 million or 4.6% of the existing capital base.
- *Deploy.* Incremental capital can be deployed with a variety of balance sheet actions that preserve the current 14.6% total RBC ratio:
 - Issue a special dividend of \$1.32 per share
 - Repurchase 45,114 shares, increasing EPS \$0.15 or 5.6%
 - Organically grow assets by \$10 million

Capital Savings Percentile



Capital Metrics and Management

| | | |
|---|---------|----------|
| Total Assets (millions) | \$229 | |
| Gross Income Margin | 4.5% | |
| Tangible Common Equity | 9.7% | |
| Leverage Ratio | 9.4% | |
| Capital Estimates | Current | Basel II |
| Tier 1 RBC | 13.3% | 13.9% |
| Total RBC | 14.6% | 15.2% |
| Potential Use of Basel II Capital Savings | | |
| Special Dividend (\$/share) | \$1.32 | |
| Share Repurchase (7/29/2008 price) | | |
| Number of Shares | 45,114 | |
| Change in EPS | \$0.15 | |
| Organic Asset Growth (millions) | \$10 | |

Asset Mix



Upon request, Second Pillar Consulting can provide similar information for all 63 West Virginia banks free of charge

West Virginia 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 |
| Bank of Mount Hope, Inc. | Mount Hope | \$ 112,591 | \$ 1,535 | 17.0% |
| Calhoun County Bank, Inc. | Grantsville | \$ 100,000 | \$ 1,437 | 16.8% |
| Guaranty Bank & Trust Company | Huntington | \$ 144,866 | \$ 1,984 | 16.2% |
| First Sentry Bank, Inc. | Huntington | \$ 321,027 | \$ 3,581 | 16.1% |
| Main Street Bank Corp. | Wheeling | \$ 191,252 | \$ 2,216 | 15.4% |
| First Neighborhood Bank | Spencer | \$ 131,859 | \$ 1,572 | 13.9% |
| First Bank of Charleston, Inc. | Charleston | \$ 140,477 | \$ 1,394 | 13.5% |
| First Federal Savings and Loan Association | Ravenswood | \$ 7,769 | \$ 134 | 13.4% |
| Pleasants County Bank | Saint Marys | \$ 53,803 | \$ 762 | 12.4% |
| First Exchange Bank | Mannington | \$ 183,093 | \$ 1,640 | 12.3% |
| Williamstown Bank, Inc. | Williamstown | \$ 99,487 | \$ 1,277 | 12.0% |
| Freedom Bank | Belington | \$ 142,433 | \$ 1,465 | 11.7% |
| Citizens Bank of Weston | Weston | \$ 167,384 | \$ 1,724 | 10.1% |
| First National Bank of Williamson | Williamson | \$ 94,788 | \$ 1,161 | 10.1% |
| Citizens Bank of Morgantown, Inc | Morgantown | \$ 33,298 | \$ 521 | 10.0% |
| Cornerstone Bank, Inc. | West Union | \$ 74,040 | \$ 1,088 | 9.8% |
| West Union Bank | West Union | \$ 100,480 | \$ 1,040 | 9.6% |
| First State Bank | Barboursville | \$ 175,426 | \$ 1,528 | 9.5% |
| Union Bank | Middlebourne | \$ 171,578 | \$ 967 | 9.2% |
| Hancock County Savings Bank, FSB | Chester | \$ 276,655 | \$ 3,668 | 9.2% |
| Averages | | \$ 136,115.30 | \$ 1,534.77 | 12.4% |

Source: 2008Q3 Call Reports; SPC estimates

West Virginia 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 |
| CNB Bank, Inc. | Berkeley Springs | \$ 285,276 | \$ 937 | 3.7% |
| Logan Bank & Trust Company | Logan | \$ 221,350 | \$ 712 | 3.3% |
| First National Bank of Peterstown | Peterstown | \$ 46,107 | \$ 155 | 3.1% |
| Fayette County National Bank of Fayetteville | Fayetteville | \$ 76,179 | \$ 242 | 2.9% |
| Mountain Valley Bank, NA | Elkins | \$ 105,332 | \$ 417 | 2.8% |
| Bank of Gassaway | Gassaway | \$ 161,765 | \$ 560 | 2.7% |
| Northern Hancock Bank & Trust Company | Newell | \$ 28,880 | \$ 77 | 2.4% |
| FNB Bank, Inc. | Romney | \$ 133,720 | \$ 280 | 1.8% |
| Pendleton Community Bank | Franklin | \$ 202,128 | \$ 449 | 1.6% |
| City Holding Company | Charleston | \$ 2,465,525 | \$ 2,273 | 0.9% |
| Whitesville State Bank | Whitesville | \$ 63,542 | \$ 56 | 0.8% |
| Progressive Bank, National Association | Wheeling | \$ 261,646 | \$ (31) | -0.1% |
| First Century Bank, National Association | Bluefield | \$ 421,284 | \$ (33) | -0.1% |
| Harrison County Bank | Lost Creek | \$ 82,139 | \$ (40) | -0.5% |
| Summit Financial Group, Inc. | Moorefield | \$ 1,567,039 | \$ (849) | -0.7% |
| First Peoples Bank, Inc. | Mullens | \$ 120,324 | \$ (143) | -0.7% |
| Jefferson Security Bank | Shepherdstown | \$ 239,150 | \$ (202) | -0.9% |
| Miners & Merchants Bank | Thomas | \$ 43,550 | \$ (221) | -3.1% |
| Bank of Charles Town | Charles Town | \$ 293,907 | \$ (1,189) | -3.6% |
| Doolin Security Savings Bank, FSB | New Martinsville | \$ 41,684 | \$ (416) | -7.3% |
| Averages | | \$ 343,026 | \$ 152 | 0.5% |

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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