Predicting the Next Big Banks to Exit TARP

by: Linus Wilson June 06, 2010 | about: ASBC / BAC / BK / BPOP / C / CRBC / EWBC / FBP / FHN / FITB / FULT / GS / JPM / KBE / MI / MS / MTB / RF / STI / STT / WFC / WL / WTNY / XLF / ZION

The big surprise with the bank bailouts is that we got so much money back so soon. The banks recoiled from the stigma of Troubled Asset Relief Program (TARP) and the first eight TARP recipients paid back a combined $140 billion plus dividends and warrant proceeds. The first eight bailed out banks were Bank of America (BAC), Citigroup (C), JPMorgan Chase (JPM), Wells Fargo (WFC), Goldman Sachs (GS), Morgan Stanley (MS), State Street (STT), and Bank of New York Mellon (BK).

While these banks looked better than their smaller rivals with respect to some risked based Basel capital metrics, they lagged by over four percent behind their smaller rivals in simpler leverage ratios based on total bank assets. These big banks had 40-to-1 leverage using the tangible common equity (TCE) to total assets leverage ratio at the end of 2008.

The other TARP recipients had leverage ratios closer to 6.4 percent, or 16-to-1, according to table 3 of my new coauthored paper. The stress test, the preferred for common swap of Citigroup in July 2009, and the capital raises of 2009 did not completely close this gap. Thus, I believe this lends some support to the Collins amendment of the Senate version of the financial reform bill that says the big banks have to be held to the same standards as the small banks.

In total 55 publically traded banks out of 282 receiving taxpayer funds exited TARP in 2009. My new paper "Escaping TARP" written with Professor Wendy Wu of Wilfrid Laurier University in Canada predicts which banks will exit TARP. Here I have applied the paper's results to all the banks with investments exceeding $300 million, which have not yet fled the TARP.

Two of the three banks that were the least likely to exit TARP have seen private buyers come in to save the banks on the condition that the U.S. Treasury will take huge haircuts on its investment. In both cases, the buyout happens at a fraction the pre-deal stock price so other equity holders take a big hit too. One bank is the South Financial Group (TSFG) which received $347 million from taxpayers and has a deal pending with TD Bank. The other is Sterling Financial Corporation (STSA) of Washington, which received $303 million from TARP and has an investment pending with the private equity firm Thomas Lee Partners.

Below are the banks that are most likely to exit TARP, according to the model, which have yet to pay back any money. These are banks that the model predicted had a high chance of exiting TARP. They are ordered from the best chance of exiting to the least likely to exit TARP.

	Most Likely to Exit TARP	2008 Assets in MM	TARP Funds in MM
1	ASSOCIATED BANC-CORP (ASBC)	$24,192	$525
2	M&T BANK CORPORATION (MTB)	$65,816	$600
3	FULTON FINANCIAL CORPORATION (FULT)	$16,185	$376
4	EAST WEST BANCORP (EWBC)	$12,423	$307
5	WHITNEY HOLDING CORPORATION (WTNY)	$12,381	$300
6	WILMINGTON TRUST CORPORATION (WL)	$12,319	$330
7	SUNTRUST BANKS, INC. (STI)	$189,138	$4,850
8	ZIONS BANCORPORATION (ZION)	$55,093	$1,400
9	FIRST BANCORP (FBP)	$19,491	$400
	Total	**$407,037**	**$9,088**

Thus, the model picks SunTrust (STI), Zions (ZION), and M&T Bank (MTB) as the most likely banks to leave with assets above $50 billion.

The banks below have a zero to 20 percent chance of exiting TARP, according to the model. I omitted TSFG and STSA, which have restructurings pending, which also mean massive taxpayer losses. The banks that the model says that are least likely to exit TARP are the following, which are ordered from least likely to most likely to leave the program:

	Least Likely to Exit TARP	2008 Assets in MM	TARP Funds in MM
1	MARSHALL & ILSLEY CORPORATION (MI)	$62,336	$1,715
2	POPULAR, INC. (BPOP)	$38,883	$935
3	CITIZENS REPUBLIC BANCORP, INC. (CRBC)	$13,086	$300
4	FIFTH THIRD BANCORP (FITB)	$119,764	$3,408
5	FIRST HORIZON NATIONAL CORPORATION (FHN)	$31,022	$867
6	REGIONS FINANCIAL CORP. (RF)	$146,248	$3,500
	Total	**$411,339**	**$10,725**

Marshall & Ilsley (MI), Fifth Third (FITB), and Regions (RF) are the least likely banks with over $50 billion in assets to exit TARP. Nevertheless, Regions and Fifth Third's managers have made public statements about their desire to exit TARP.

The model uses new capital raises, Tier 1 capital ratios, ROA, bank size, and non-performing asset ratios among other variables to predict bank exit. (I used model 2 in table 5 for these estimates if you are interested.)

While the model can be a useful tool to help predict which banks leave TARP, I think other less quantitative factors are also good predictors of whether a bank will exit

TARP. If the bank’s management says they want out of TARP as soon as possible and says how they are taking steps to make that happen, then I would be inclined to rely on those statements as much or more than any statistical model. Yet, I would be more confident of a bank’s likelihood of exit if both the model and the public statements were in agreement. The model uses bank ratios so it excludes the insurance companies such a Lincoln National (LNC), which I think, based on subjective criteria, will exit TARP before the end of the year. I would be happy if the model is right and all the top list banks leave the TARP early. Nevertheless, I hope many of the banks on the bottom list banks prove me wrong and payback the funds early, too.