CONSUMER BANKERS ASSOCIATION

leaders in retail banking

Testimony of

CATHLEEN H. NASH

On Behalf of the

CONSUMER BANKERS ASSOCIATION

Before the

Committee on Financial Services

And the

Committee on Small Business

United States House of Representatives

February 26, 2010

TESTIMONY OF CATHLEEN H. NASH
PRESIDENT & CEO, CITIZENS REPUBLIC BANKCORP
ON BEHALF OF THE CONSUMER BANKERS ASSOCIATION
BEFORE THE COMMITTEE ON FINANCIAL SERVICES
AND THE COMMITTEE ON SMALL BUSINESS
UNITED STATES HOUSE OF REPRESENTATIVES

"CONDITION OF SMALL BUSINESS AND COMMERCIAL REAL ESTATE LENDING IN LOCAL MARKETS"

Good afternoon Chairman Frank, Chairwoman Velázquez, ranking member Bachus, ranking member Graves and members of the Committees, my name is Cathy Nash and I am the President and CEO of Citizens Republic Bancorp (a $12 billion bank headquartered in Michigan and serving the upper Midwest). I am also a member of the Board of Directors of the Consumer Bankers Association (CBA). For more than 90 years, CBA has been the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in all areas of consumer financial services, including small business lending. CBA members include most of the nation's regional and super community banks, as well as the largest bank holding companies that collectively hold two-thirds of the industry's total assets.

I am pleased to have this opportunity to appear before you today to discuss the issues surrounding small business and commercial real estate lending. As we seek to continue to move our economy, indeed our country, back on the path of stability and prudent growth, it is important to seek input and engage in vigorous debate with those most able to influence that path.

In my positions with Citizens Republic and CBA, I see that the challenges we face in serving our clients, protecting our depositors and navigating through the current economic climate have been magnified. As a bank we ask, how much capital is enough? Some would now say, in the view of the crisis we experienced, that a bank can never have too much capital. With an uncertain view of the near future, regulators must focus on protecting the bank's depositors. The best way to do that is require banks to hold more capital. However, every dollar of capital a bank carries to cover a potential bad loan is a dollar that cannot be lent to a business owner. It is a dollar that cannot help a community recover and grow by adding jobs.

It is exactly the holding of more capital that adds to the cycle's length and severity. By holding capital and therefore making fewer loans, or actively shrinking the bank's balance sheet to preserve even more capital, businesses cannot grow and hire because their capital access has been restricted.

As banks have navigated through this cycle, it is clear that some of the practices of the last decade must be curtailed and this impacts those businesses seeking to borrow today. In the past, banks competed vigorously for new loan clients. While most banks had strong credit criteria and policies, too often those were overridden to "win" a deal. In today's environment, we have not loosened nor tightened our standards. We are holding every loan opportunity up against those policies. This may feel to a borrower as if the bank is getting more restrictive when, in fact, we are following long-established policies.

In our markets, we saw some banks close credit lines via letters that clients brought into our branches. We have seen competitors exit industry segments and geographies. For business clients, we look at each borrower discretely. Based on their plans and forecasts, we have tried to size our lines of credit based on their business need. For example, a long standing client with a $2 million line of credit that has never been drawn down causes the bank to hold capital against that line, although never used. So we might work with that client to reduce the line to better match their business needs and forecasts. To some clients, this may feel like a significant reduction. Our goal continues to be to ensure we meet our clients' needs and manage our capital requirements.

Commercial real estate lending is driven by lower occupancy and/or lower rents paid by tenants or on the building side, slower sales that result in lower prices. These factors in turn drive the appraisal of the properties and our ability to lend to the level that we originally thought we could. For example: we have a client who wants to build an office building -- a $10 million project. Presales did not come through and those that did were at lower rent rates. Our client believes the market will "come back" but is unwilling to put in additional money to maintain the loan-to-value that we look for per our credit policy.

Recent changes and proposals have been made that should have a positive impact. Last fall, the FFIEC's policy statement on Commercial Real Estate Loan workouts was issued. I do not believe this was issued with the intention to increase commercial real estate lending, but rather to provide guidance on how to manage those commercial real estate clients you have that are faced with devalued property. Simply put, we don't have to move a project that has cash flow into non-performing simply because the appraisal of the property is lower. We were encouraged to complete the analysis of our portfolio by our regulators. As to whether the regulators supervision has been consistent – we are just entering our loan review exam with our regulators, so that remains to be seen.

Finally, the president's recent proposal and HR 3854, with proposed changes to SBA loans, are also positive steps. Providing revolving working capital – this primary use of SBA express loans is more critical today than ever – by increasing the limit to $1 million on those loans, allows us to work with an even greater pool of borrowers to properly position them to successfully navigate the next few years in this cycle.

The president's second proposal, to allow for refinancing of owner occupied commercial real estate loans under the SBA 504 program, is also a very positive move. Today, those loans cannot be used to refinance maturing debt. This change opens the door for borrowers to access long term fixed rates (20 year fixed for 40% of the loan need), something very important in an uncertain time and a view of rates eventually rising.

Without going into a review of each HR 3854's provisions, generally the increase in 7(a) loans from $2 to $3 million is good, but could have a much greater impact, since it is allowable for debt refinance, if it was expanded to $5 million. The 90% guarantee on the 7(a) loans as well as simplifying the process will get more banks participating in the program, so that is also a positive.

The ARC Loan program is well intended but may not be enough to get bankers to use it, as it essentially asks the bank to certify that the borrower is in financial hardship and at the same time certify that the borrower will be able to pay the debt back to qualify for the loan.

In your invitation, you asked how banks can, as a practical matter, best fulfill their fundamental role as intermediaries in the credit markets consistent with prudent lending standards and strong capital requirements in a period of extreme financial and economic stress. That is indeed the key question. Good borrowers, who have the willingness and capacity to repay, will always find a loan. Those borrowers with weaker financials will find it more difficult to meet the credit requirements of their bank. The fundamentals of capacity and willingness to repay must be established once again as a hallmark of lending activity. This will happen, one borrower at a time, by bankers who know and understand them. We thank you for continuing to look for ways to improve small business and commercial real estate lending. The CBA is committed to working with the members of both committees to achieve this goal.