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Conference Chatter

Bank, Thrift & Asset Manager - Industry News

It's a private equity affair

BLOG

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At the SNL Bank M&A Symposium this week, one of the major topics of discussion was the role private equity has to play in the banking sector, whether through acquisitions of failed banks or investments in existing banks.

There has been some regulatory squabbling over whether private equity should have a seat at the bidding table for failed banks. The FDIC has taken the stance that private investments in failed institutions should come with more stringent restrictions, including higher capital requirements. The OCC on the other hand seems to favor the idea of private equity entering the bank space. It has granted shelf charters to private equity groups, but none of those groups have yet acquired banks.

Some private equity investors at the SNL event chafed at the FDIC's restrictions, saying that having to maintain higher capital levels creates an uneven playing field, putting private equity firms at a disadvantage when acquiring banks.

Nicholas Paumgarten, the chairman of Corsair Capital LLC, said the pricing disadvantage made it unlikely that his fund would be successful in the bidding process against other banks and thrifts.

On the other hand, John Oros, managing director at J.C. Flowers & Co. LLC, said his company remains extremely active in the bidding process, despite the restrictions. The company has scored one success already, leading the private equity group that acquired IndyMac, now OneWest, from the FDIC in January.

The problem, Oros said, is not the restrictions that the FDIC has placed on private equity, but rather the areas where the FDIC policy statement, which gives the agency latitude to waive some requirements, is less than clear. Those uncertainties, and other unknowns surrounding transactions, are critical in determining whether J.C. Flowers could do another deal.

Some private equity groups that have become bank holding companies do not have to comply with the more stringent regulations, such as Eggemeyer Advisory Corp. unit Castle Creek Capital LLC. At the conference, Castle Creek managing principal William Ruh said he would prefer that his fund was not a holding company, because it is "restrictive." However, because Castle Creek wanted to have an "active role" in the banks that it invests in, registering as a bank holding company became necessary.

However, Credit Suisse vice chairman of mergers and acquisitions David DeNunzio noted that much of the private equity capital looking to invest in banks has little experience with financials. Those firms look at banking as an industry that has been "beaten down and depressed," DeNunzio said, adding that it is not all that easy to make money in the sector, as TPG Inc. found out with its investment in Washington Mutual Inc.

Oros pointed out that private equity firms could approach the banking industry from two different extremes. The first, which he called "the melting ice cube scenario," entails stripping the franchise of value. On the opposite end of the spectrum, the ownership group could look to build a much stronger bank, which has the possibility of boosting profits substantially over time.

"When you buy a troubled bank, you get two things," Oros said. "You get a bank, and you get trouble."

It is not clear whether every private equity firm could bid on a troubled bank, or if they would even want a seat at the FDIC's table. But there are other ways for private equity to participate in the bank space.

For example, private equity can enter the industry through minority investments, as when Warburg Pincus & Co. agreed in July to make a $115 million investment in Webster Financial Corp.

Another way that private equity has entered the space is through side-by-side public and private offerings. In those deals, a private equity firm performs due diligence and commits to injecting capital into the institution contingent on the successful completion of the public offering. The private equity firm's commitment, in effect, serves as a blessing for the public offering.

Sandler O'Neill & Partners principal Emmett Daly said Seacoast Banking Corp. of Florida's recent capital raise was one of those transactions. He said that when the company first sought to raise capital, the public capital markets were still closed for smaller institutions like Seacoast. As a result, the capital raise started as a private transaction. By June, however, the public markets had opened, allowing a hybrid solution.

In the end, Seacoast sold $13 million in common stock to CapGen Financial Partners, which "validated" the company in the eyes of other investors, Daly said. Seacoast then raised an additional $66 million in the public offering that followed.

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