As seen in the Santa Clarita Valley Business Journal – April 2009

Financial Alphabet Soup Spells Confusion

Over the past several months, we have all been asked to expand our vocabulary of acronyms exponentially. What does NFSP, EESA, TARP, CPP, SSFI, MBS stand for – let alone how they (*are supposed to*) function is a tremendous amount to process… particularly when the vast majority of us are still reeling from the diminishing balances in our retirement accounts, the decreasing value of our homes and ever increasing costs at the grocery store! With that in mind, I thought that the following brief description / explanation of a few of these terms might prove helpful:

The Troubled Asset Relief Program – TARP is a broad economic relief program that has many "moving" parts. Authorized by Congress in early October of 2008 through the *Emergency Economic Stabilization Act* (EESA), the original purpose of TARP was to purchase troubled assets of *Systemically Significant Failing Institutions* (SSFI), thus promoting greater financial stability, unlock frozen credit markets, improve liquidity and restore confidence in our nation's financial institutions. Initially TARP provided the U.S. Treasury oversight of the purchasing power of $700 billion to buy up mortgage backed securities (MBS) from institutions across the country – in reality, this has yet to occur. No "***Troubled Assets***" have been purchased by the U.S. Treasury, not from AIG, General Motors, Fannie Mae or Freddie Mac. *However, the Federal Reserve Bank has committed to the purchase of $1.25 trillion in mortgage-backed securities this year, though these funds are not associated with TARP.*

In sharp contrast to its original purpose, the TARP policy immediately shifted to include the injection of capital into the SSFI banks (as demonstrated when the leaders of our nation's 9 largest banking institutions were called to Washington and *requested* to accept capital injections). A short time later, the Capital Purchase Program (CPP) emerged to address the needs of **financially stable U. S. banks for additional capital to continue their lending operations**. In contrast to the largest institutions that were forced to take TARP capital, banks applying under the Capital Purchase Program (CPP) are required to be healthy, well capitalized organizations.

The Capital Purchase Program – (CPP) was designed to provide capital to ***healthy financial institutions.*** CPP money is an *investment* in *financially stable banks* and is designed to promote the availability of credit – ***the absolute opposite*** of other uses of TARP funds.

The CPP is a voluntary program (*though participation has been encouraged*) wherein the United States Treasury Department invests (via the purchase of preferred stock, securities and/or warrants) in participating institutions.

In short, the terms of these investments include a 5 year agreement wherein participating banks will in essence "buy back" these shares during an agreed upon term, at an annual interest rate of 5% – after 5 years, this interest rate increases to 9% (ample incentive for participating banks to quickly repay the debt). Additionally, all participating banks agreed to meet exacting reporting criteria as to how these funds are used, as well as management doctrine including (but not limited to) executive compensation and organizational operations. The Treasury's interest in the institution ceases upon full repayment of the debt. Also important is the fact that it is expected that the investment made by our government in these banks should net our U.S. Treasury between a $40 and $45 BILLION dollar return upon repayment.

In explanation, *capital is not loaned out directly* – capital acts as a cushion against potential losses -- most of which are due to deteriorating credit quality. Banks leverage capital up to 15 times (*not the 40 times we witnessed with Lehman and other investment banks*). However for banks to be able to make loans and leverage their capital, they must have deposits. Simply stated community banks take in local deposits and lend that money to local businesses. For each dollar of capital held, a bank can lend $7 to $15 dollars, providing that the bank has an additional $6 dollars in deposits, and the bank maintains total 'risk based capital' of more than 10% of its total assets (loans and other holdings). Even in today's environment 98% of all banks are deemed as "Well Capitalized", the regulators highest available designation allowing the majority of financial institutions to easily meet this 10% ratio.

Hundreds of healthy, financially strong, community banks initially accepted the CPP funds in exchange for preferred stock, securities and / or warrants. I do not hesitate to share with you that Mission Valley Bank was one of them. Our management, Board of Directors and shareholders agreed that this infusion of additional capital would enhance our Bank's ability to aide the communities we serve. As a well capitalized, financially sound company, we eagerly accepted the capital knowing that loan demand throughout the areas we serve continues to climb – particularly now. Most unfortunate however, is the fact that due to the U.S. Treasury's ever changing restrictions and requirements now associated with the CPP, many good, strong community banks are opting to return these funds and seek alternative sources of capital.

In short, our Nation's economic crisis continues and the only thing that we can count on is the fact that before Spring turns to Summer – there will be another dozen initiatives and / or over sight committees with a whole new set of acronyms for us to learn.

Tamara Gurney is President and CEO of Mission Valley Bank – an FDIC insured, community based, business bank with two offices serving the Santa Clarita Valley. Tamara can be reached at (877) 394-2306 – www.MissionValleyBank.com

MISSION VALLEY BANK