

SR003_7: Failed Bank Report

Douglass National Bank

1670 East 63rd Street
Kansas City, MO 64110

(9/3/1983 – 1/25/2008)

Report Objective

This report has **two** objectives, using the bank's **data***

1. To examine the bank finances in the quarters prior to its failure.
2. To analyze the bank finances using our Key Performance Indicator (KPI) scoring approach to determine if the bank's failure is something we could have predicted.

*Data source: FDIC and company filings.

Bank Background

FDIC Certificate #	24660
Parent Holding Company	DOUGLASS BANCORP, INC.
Bank Charter Class	National Bank
Asset Concentration	Commercial Lending Specialization
Product Specialty	Commercial Lending Services, Personal Banking Services, Mortgage Lending Services
Number of Branches	3 (as of December 31, 2007)
Number of Employees	25 (as of December 31, 2007)

Executives

President/CEO	Lester W. Johnson
SVP	Sara J. Swaters

What took place?

Douglass National Bank, Kansas City, MO was closed by the Office of the Comptroller of the Currency on January 25th, 2008. The Federal Deposit Insurance Corporation (FDIC) was named Receiver. The estimated cost to the FDIC Deposit Insurance Fund is \$5,600,000, compared to the average cost of \$389,206,944. Liberty Bank and Trust, New Orleans, LA acquired all deposits and most assets.

Bank Financial Snapshot

Financial Data Overlay (thousands)			
	2006 Q4	2007 Q4	Percentage Change
Assets	\$68,430	\$52,824	↓ 22.8%
Liabilities	\$66,084	\$51,634	↓ 21.9%
Net Income	-\$4,265	-\$1,343	↑ 68.5%

- The average net income change for all the FDIC banks was -29.96% in the same period.
- The average net income change for all the commercial lending specialization banks was -39.23% in the same period.
- Compared with the whole industry and other commercial lending specialization banks, Douglass National Bank's loss declined significantly in 2007.
- Douglass National Bank's assets and liabilities largely declined, while the other commercial lending specialization banks had an average 7% decline in both assets and liabilities.

Key Performance Indicators

KPI Summary for 2007 Q4	
Normalized Income Rating	Moderate
Delinquent Asset Rating	Very Poor
Asset: Liability Rating	Very Poor
Real Estate Asset Rating*	Good
Bankability Composite Score	-14.17** (Very Poor)

Possible ratings: *Excellent, Good, Moderate, Poor, Very Poor.*

*This rating is relevant to the current “financial crisis” fueled by mortgage security backed loans.

**This is out of 100.

Normalized Income Analysis

	2006Q4 	2007Q1	2007Q2	2007Q3	2007Q4
Normalized Income	-4.06%	-0.80%	-0.79%	-0.18%	-0.43%
SD's from Average*	-9.90	-2.53	-2.44	-0.928	-0.730
Ranking	Very Poor	Very Poor	Very Poor	Moderate	Moderate


- Douglass National Bank had a normalized income of -0.43% in the fourth quarter of 2008, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average normalized income of 0.07%. The standard deviation of the normalized incomes was 0.69%, which means that Douglass National Bank was 0.730 SD's below the average.

*Average of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Delinquent Asset Analysis

	2006Q3 	2006Q4	2007Q1	2007Q2	2007Q3	2007Q4
Delinquent Asset	5.4324%	9.3199%	4.3259%	7.5896%	6.2029%	9.2431%
SD's from Average*	3.32	6.08	2.30	4.50	3.22	4.65
Ranking	Very Poor	Very Poor	Very Poor	Very Poor	Very Poor	Very Poor

- Douglass National Bank had a delinquent assets out of total assets ratio 9.24% in the last quarter of 2007, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average delinquent asset of 1.3829%. The standard deviation of the delinquent assets was 1.6894%, which means that Douglass National Bank was about 4.7 SD's above the average.
- Since the third quarter of 2006, Douglass National Bank's delinquent assets ratio has been very poor in relation to banks of the same asset concentration hierarchy.

*Average of banks of the same asset concentration hierarchy



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Real Estate Loan Asset Analysis

	2006Q3	2006Q4	2007Q1	2007Q2	2007Q3	2007Q4
Real Estate Loan Asset Ratio	43.52%	52.13%	46.20%	45.88%	44.08%	43.82%
SD's from Average*	-0.73	-0.15	-0.54	-0.6	-0.73	-0.77
Ranking	Good	Moderate	Moderate	Moderate	Good	Good

- Douglass National Bank had a 43.82% R/A ratio in 2007 Q4, the quarter before it failed.
- In 07 Q4, banks of the same asset concentration hierarchy (commercial lending specialization) had an average R/A ratio of 55.54%. The standard deviation of R/A ratio was 15.29%, which means that Douglass National Bank was 0.77 SD's below the average.

*Average of banks of the same asset concentration hierarchy

Asset: Liability Analysis

	2006Q3	2006Q4 	2007Q1	2007Q2	2007Q3	2007Q4
Asset: Liability Ratio	107.35%	103.55%	102.85%	101.88%	102.14%	102.30%
Median A/L Ratio*	110.56%	110.60%	111.68%	110.74%	110.97%	110.97%
Ranking	Poor	Very Poor	Very Poor	Very Poor	Very Poor	Very Poor

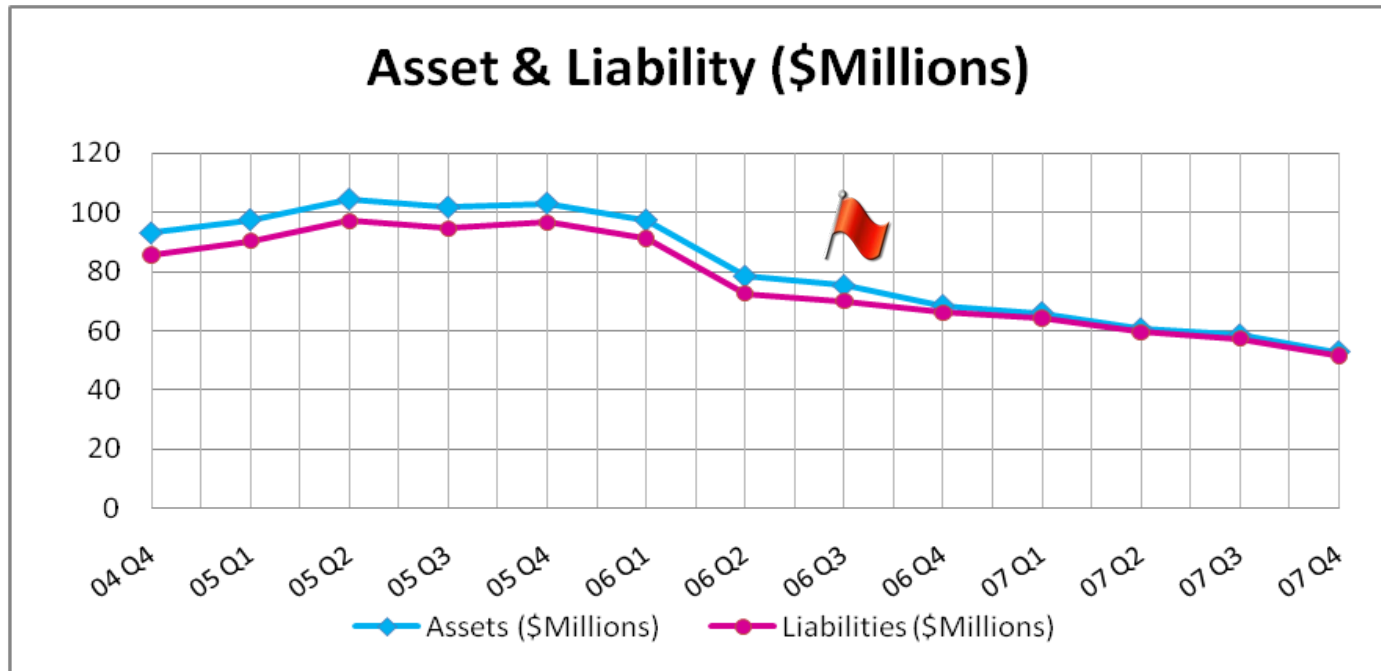
- Douglass National Bank had a nearly 4% decreased in A/L ratio in 06 Q4.
- The bank fell into the worse ranking in 06 Q4.

*Median of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Asset & Liability History

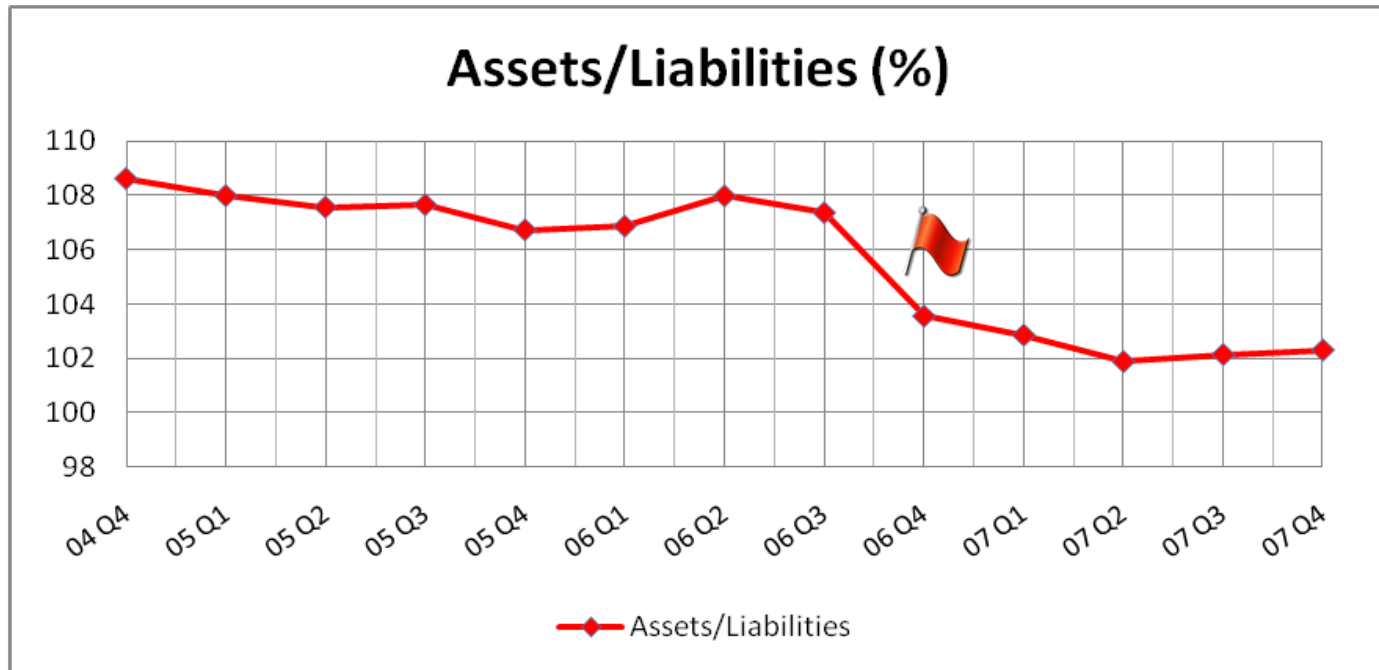


- The difference between Asset and Liability was getting closer since 06 Q3.



Indicates sign of bank in financial distress

Asset/Liability History

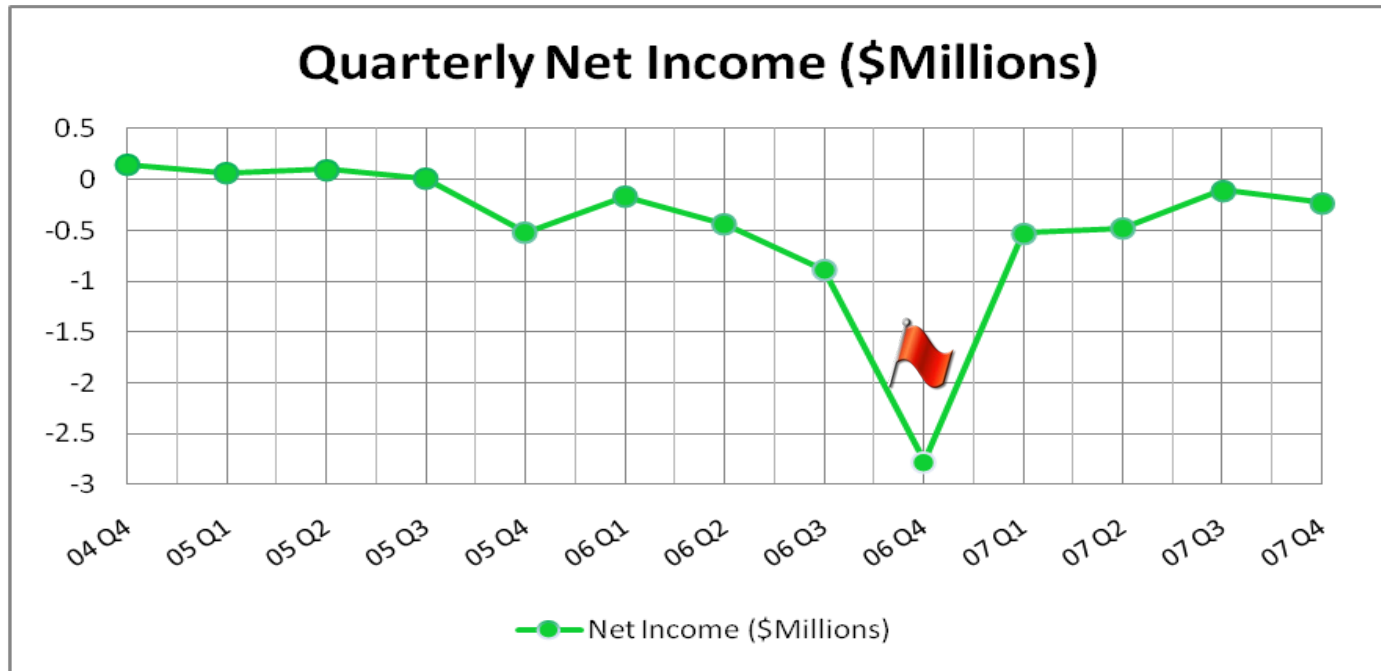


- The A/L ratio was decreasing from 06 Q2 to 07 Q2.



Indicates sign of bank in financial distress

Net Income History

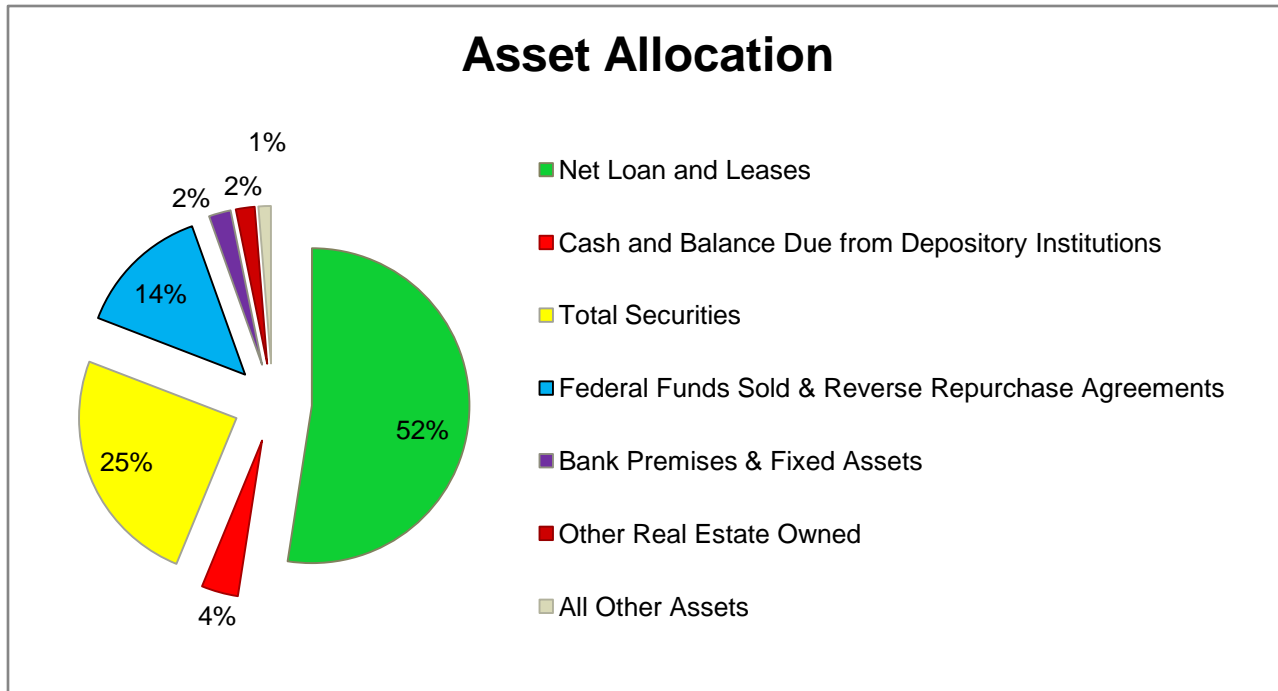


- The bank recorded a big loss in 06 Q4.
- The bank started reporting losses since 05 Q4.



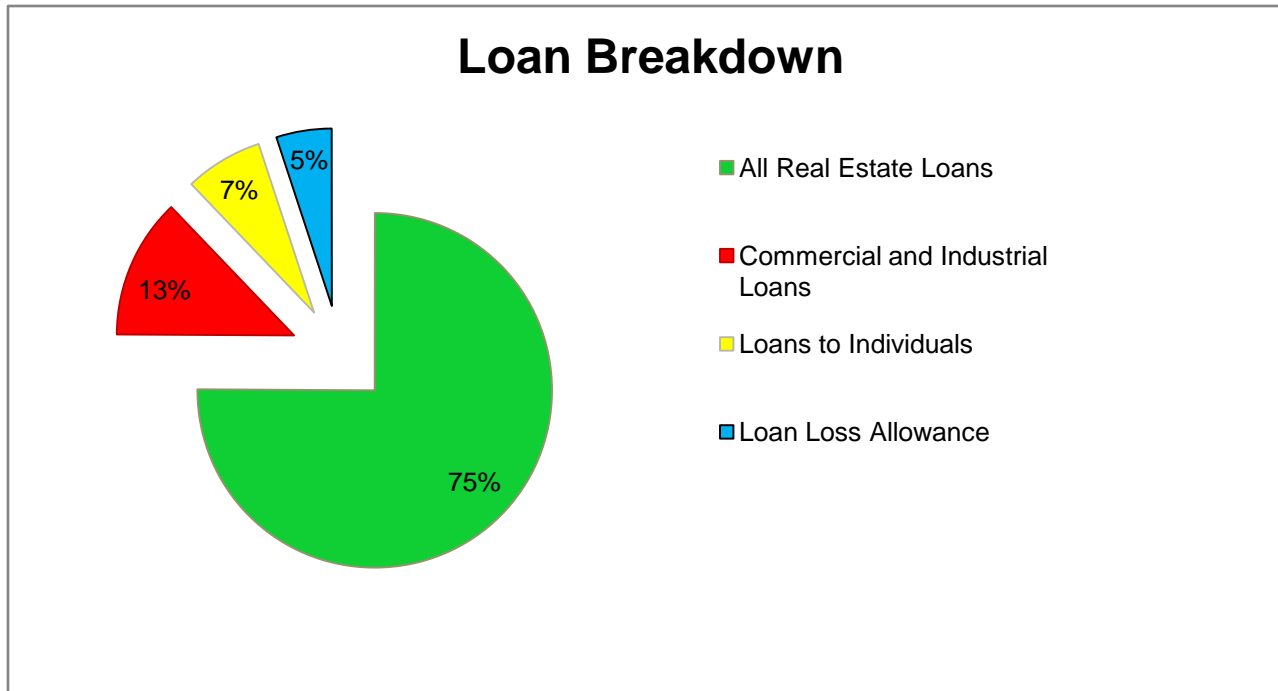
Indicates sign of bank in financial distress

Asset Allocation



- The average percentage of Net Loans for banks of the same Asset Concentration Hierarchy in the fourth quarter of 2007 was 71.92%.
- The average Net Loan percentage of all banks in the fourth quarter of 2007 was 65.45%.

Loan Breakdown



- The average percentage of Real Estate Loans for banks of the same Asset Concentration Hierarchy in first quarter of 2009 was 90.04%
- The average percentage for all banks in the first quarter of 2009 was 71.75%.

Events Timeline

- Aug. 25, 07** - Douglass National Bank lost \$479,000 during the second quarter, and pushed its losses for the year to \$1 million.
- Oct. 11, 07** - First Guaranty Bancshares Inc. announced that it would not purchase Douglass National Bank.
- Jan. 25, 08** - Douglass National Bank was closed by FDIC and all its deposit accounts were transferred to Liberty Bank and Trust Company.
- Mar. 4, 08** - SEC voted to disclose information for the secondary market ETF investors in Form N-1A.
- Mar. 7, 08** - The Fed will initiate a series of term repurchase transactions that are expected to cumulate to \$100 billion.
- Mar. 19, 08** - Fannie Mae and Freddie Mac is expected to provide support to the U.S. mortgage market, up to \$200 billion immediate liquidity.
- May 29, 08** - U.S.-Canada mutual recognition arrangement: U.S. Securities markets and certain U.S. financial service firms could gain greater freedom to operate in Canada under SEC.
- June 10, 08** - FDIC releases a supervisory letter to all banks on interest reserves that examines the risks that this underwriting practice presents.
- June 11, 08** - SEC voted on a comprehensive series of credit rating agency reforms to bring increased transparency to credit rating process.
- June 17, 08** - New HOPE NOW guidelines to deal with issues surrounding second mortgages and short sales.

Events Timeline

- June. 26, 08** - FDIC adopts Basel II-Based Standardized Approach as an alternative risk-based capital framework available to all banks except the largest and most complex banks
- June. 26, 08** - FRS, FDIC, and OCC issued the host state loan-to-deposit ratios, which help indicate branches outside of the home state that were established or acquired for the purpose of deposit production.
- Jul. 13, 08** - Paulson Announces a three-part plan for GSEs: a temporary increase in the line of credit, a temporary authority for Treasury to purchase equity, and an advisory role is given to the Fed.
- Aug. 20, 08** - FDIC's implementation in Loan Modification Program will help to modify troubled IndyMac mortgages loans.
- Sept. 17, 08** - SEC clarified that bank support of money market mutual funds generally are not required to present the fund on-balance sheet, but disclosure of the nature of the support provided is expected.
- Sept. 18, 08** - SEC requires that certain institutional money managers report their new short sales of certain publicly traded securities.
- Sept. 19, 08** - SEC prohibited short selling in 779 financial institutions.
- Sept. 20, 08** - Treasury Secretary Hank Paulson releases \$700 billion proposal to purchase troubled mortgage-related assets.
- Oct. 7, 08** - Emergency Economic Stabilization Act of 2008 Temporarily Increases Basic FDIC Insurance Coverage from \$100,000 to \$250,000 per Depositor.
- Oct. 14, 08** - FDIC creates new program to guarantee bank debts and fully insure non-interest bearing deposit transaction accounts.

Events Timeline

- Oct. 14, 08** - The Treasury Department will invest up to \$250 billion in the nation's banks via the Capital Purchase Program.
- Nov. 20, 08** - FDIC announces the availability of IndyMac Loan Modification Model.
- Nov. 25, 08** - Created the Term Asset-Backed Securities Loan Facility to support the issuance of asset-backed securities collateralized by loans.
- Dec. 3, 08** - SEC approved measures to strengthen oversight of credit rating agencies.
- Dec. 16, 08** - Troubled banks have to provide certain position level and counterparty level data and QFC counterparty and portfolio identifiers to FDIC in a timely manner.
- Dec. 23, 08** - Treasury provides TARP funds to focal Banks by purchasing \$2.8 billion investment from 49 banks.
- Dec. 30, 08** - The Fed announced that it will purchase mortgage-backed securities.
- Jan. 15, 09** - The Senate voted to allow access to the remaining bailout funds of \$350 billion.
- Jan. 27, 09** - As part of the Capital Purchase Program, Treasury announced investments of \$386 million in 23 healthy banks.
- Feb. 10, 09** - Geithner rolls out the Financial Stability Plan, promises to perform "stress tests" on big banks, and commit \$100 billion to boost the TALF.
- Feb. 10, 09** - A Capital Assistance Program to help ensure banks hold sufficient capital, produce a more consistent and forward-looking assessment of risks on banks' balance and their potential capital needs.
- Feb. 10, 09** - A Public-Private Investment Fund will combine public and private capital with government financing to help free up capital to support new lending.

Events Timeline

- Feb. 10, 09** - Treasury and Fed expanded the Term Asset-Backed Securities Lending facility up to \$1 trillion.
- Feb. 18, 09** - President Obama signs the American Recovery and Reinvestment Act of 2009, which limits bonuses of the highest earning executives.
- Mar. 4, 09** - Treasury announced loan modification guidelines under the Administration's Homeowner Affordability and Stability Plan.
- Mar. 23, 09** - Using TARP capital and capital from private investors, the Public-Private Investment Program will generate \$500 billion in purchasing power to buy legacy assets.
- May 29, 09** - FDIC tightens the deposit interest rates paid by banks that are less than well capitalized. Generally, such banks will be permitted to offer to "national rate" plus 75 basis points.
- June 9, 09** -10 Of the largest U.S financial institutions are expected to make CPP repayments to Treasury.
- Jul. 2, 09** - FDIC proposed guidelines require private equity firms to hold bank purchases for 3yrs and maintain capital levels.

Report Summary – *Surprise?*

Based on the methods with which we analyzed, Douglass National Bank, its failure was **not a surprise**.

Here are the indications that Douglass National Bank should fail:

- 1) **Douglass National Bank's normalized income was always negative. Especially in 06 Q4, it lost over 4% of its total asset.**
- 2) **Delinquent Loan was ranked very poor in all 6 quarters. Especially in 06 and 07 Q4, its delinquent asset ratio almost hit 10%.**
- 3) **Douglass National Banks asset: liability ratio was ranked very poor in the last 5 quarters prior to failure. Not only that, in that 5 quarters the ratio are all below 104%.**
- 4) **Its Bankability Composite Score was -14.17 before its failure, which was considered to be very poor.**

The combination of all these four measures being poor obviously shows that the bank could fail anytime.

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Contact Information

For additional information regarding this report series, you can contact us at:

By E-mail:

info@moneyeconomics.com

By Mail:

Money Economics
P.O. Box 587
Alameda, CA 94501

By Phone:*

510.550.1694

**For media inquiry only please.*