Pension funds back buy-out fight over bank deals

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A coalition of large US state pension funds has backed the private equity industry's opposition to new rules on takeovers of troubled lenders, saying the plan would have a "chilling effect" on attempts to revive the country's banking system.

The warning by funds from states including New York, New Jersey and Oregon, which manage billions of dollars on behalf of public workers and are big investors in private equity, will strengthen the buy-out industry's lobbying against the proposed measures.

Under the planned rules, unveiled by regulators last month, private equity groups that buy a troubled bank would have to maintain its tier one capital ratio – a measure of financial strength referring to a bank's equity capital and reserves – to 15 per cent of assets. This would be three times the level of other banks. Buy-out funds would also be banned from selling their lenders for three years.

Executives argue that the rules would deter private equity from investing in failing lenders just as regulators are scrambling to find buyers for regional banks hit by the crisis.

In a letter to the Federal Deposit Insurance Corporation, which is to decide on the rules in the next few weeks, the state pension funds say the measures would have "a chilling effect on private capital participation in the acquisition of failed banks".

"The 15 per cent capital requirement is unduly restrictive and will limit the ability of these banks . . . to be recapitalised," write the investors, which include funds from Connecticut, North Carolina, Pennsylvania, Florida and Missouri. "The combined effect of discouraged participation, low-ball bids and induced focus on high-risk activities would make this programme unsuccessful.

The FDIC has indicated it might lower the capital requirement in its final rules – partly because another banking regulator, the Office of the Comptroller of the Currency, has also raised concerns about the proposals – but has not said to what level.

Private equity bidders have not been a factor in the auctions of failing banks in recent months.

No buy-out fund is believed to have bid for Colonial, an Alabama-based bank that was sold to BB&T, another regional lender, last week.

Private equity firms are also not expected to feature among the lead bidders for Guaranty Financial, a struggling Texas bank which is being sold by the FDIC.

Private equity firms' opposition to the new rules is heightened by the fact they have struggled to find lucrative investment opportunities since the onset of the financial crisis cut off their supply of cheap debt. Many had hoped to be able to put some of their vast funds to work on failing banks.

In its comments to the FDIC, for example, Lone Star, a large private equity firm that has spent $60bn buying distressed banks and other financial assets around the world, said the proposed rules displayed a "strong bias against, and suspicion of, 'private' capital".

Financial Times, London, Aug. 19th 2009, Companies, online.