

FIN 468—FALL 2007 SYLLABUS

COURSE NUMBER: FIN 468W.01

COURSE TITLE: Commercial Banking

INSTRUCTOR: James B. Bexley, Chair, Smith-Hutson Endowed Chair of Banking

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OFFICE HOURS: Tu & Th 8:00 a.m. to 11:00 a.m.
Other times by appointment.

REQUIRED TEXT: *Bank Management, Text and Cases, Fifth Edition, 1998*
George H. Hempel & Donald G. Simonson

DESCRIPTION OF COURSE: Operation of commercial banks, trust companies, Federal Reserve Banks, and other credit institutions. Federal Reserve Banks, and other credit institutions. Federal Reserve Board and its function, rediscounting, open market operations, types of notes issued, and their relation to the Federal Reserve System is stressed. Special attention is given to recent bank legislation. Cases will be used to amplify text materials.

OBJECTIVES: The major objectives of this course are:

1. To acquaint students with the roles of banks in the financial services industry.
2. To introduce students to banking theory and bank management.
3. To introduce students to specific aspects of the financial services industry.

PREREQUISITES: FIN 334 and FIN 367.

CLASS MEETINGS: Classroom BA 106 on Monday and Wednesday, 9:30 a.m. to 10:50 a.m. with the first class meeting on Monday, August 20, 2007, and the final exam Wednesday, December 12, 2007 from 8:00 am to 10:00 am.

*See University calendar.

TEACHING METHOD: The teaching methods utilized will be lecture, class discussion, problem analysis, case study, class research and presentations. To introduce an element of practicality into the learning experience, the class will be divided into groups for cases, research papers, and presentations. Students will be allowed to select topics, subject to approval of the professor. A written paper and an oral presentation will be required of each student in the group.

COURSE EVALUATION PROCESS: There will be three unit examinations and a final examination. In addition there will be outside assignments, a research paper to turn-in and an oral presentation to be made on the research paper. Grade weighting will be as follows:

Examination #1	15%
Examination #2	15%
Examination #3	15%
Case preparation and presentation	15%
Research paper/oral presentation	20%
Final Examination	20%

Course grades are determined by applying the following scale to a student's weighted average:

90 and above	A
80 to 89	B
70 to 79	C
60 to 69	D
Below 60	F

MISSED EXAM/LATE ASSIGNMENTS: No makeup exam will be given. If an exam is missed, a grade of zero (0) will be assigned for the exam. Each student will be allowed to drop the lowest exam grade and the weight of that exam will be added to the weight of the final exam. If more than one exam is missed, a score of zero (0) will be retained for those missed exams. Assignments must be turned in on the date due. No late assignments will be accepted for credit.

RELIGIOUS HOLY DAYS POLICY: Students who are absent from class for observance of a religious holy day will be allowed to take an examination or turn-in an assignment schedule for that day prior to the absence. By September 6th, the student must notify the professor in writing of each scheduled class day that he/she will be absent for a religious holy day.

ATTENDANCE: Class attendance will be checked for each scheduled class. Perfect attendance will earn 3 bonus points added to the grade computation described above. **Two class periods which equal 3 hours (each class is considered 1 and 1/2 hours) can be missed without penalty, except examination days and presentation days. For each hour missed from the fourth through the seventh, 1-point will be subtracted from the final grade for each hour missed. Absences totaling eight hours or more will result in a grade of F for the course. Three late class arrivals will be treated like one hour's absence and one point will be deducted from the final average.**

HANDICAPPED STUDENT POLICY: It is the policy of Sam Houston State University that no otherwise qualified disabled individual shall, solely by reason of his/her handicap, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any academic Student Life program or activity. Handicapped students may request academic

assistance when needed from a Committee for Continuing Academic Assistance for Disabled Students by visiting the Director of the Counseling Center in the Lee Drain Building Annex, or by calling extension 4-1720.

TENTATIVE SCHEDULE: Set out below is a tentative schedule that is subject to change:

<u>DATES</u>	<u>SUBJECT</u>
Aug. 20th	Administrative Issues & Introduction to Banking
Aug. 22nd	Chapter 1 The Changing Nature of Banking in the U.S. & Case #1
Aug. 27th	Turn in Topics , Chapter 2 Understanding a Bank's Financial Statements & Case #2
Aug. 29th	Chapter 3 Evaluating a Bank's Returns, Risks, & Overall Performance & Chapter 4 Foundations of Value in Banking & Case #3
Sep. 3rd	Labor Day Holiday
Sep. 5th	Chapter 5 Asset & Liability Management & The Yield Curve & Case #4
Sep. 10th	Exam #1 (Chapters 1-5, notes & lecture)
Sep. 12th	Chapter 6 The Acquisition & Cost of Bank Funds & Case #5
Sep. 17th	Chapter 7 Measuring & Providing Reserves & Liquidity & Case #6
Sep. 19th	Chapter 8 Managing The Security Portfolio Case #7
Sep. 24th	Chapter 9 Managing Bank Capital & Case #9
Sep. 26th	Chapter 10 The Bank Credit Organization & Case #10
Oct. 1st	Topic #1 Written Reports Due, Case #11 & Guest Bankers
Oct. 3rd	Exam #2 (Chapters 6-10, Commercial Lending, notes & lecture)
Oct. 8th	Topic #1 Oral Presentations
Oct. 10th	Case #12 & Commercial Lending
Oct. 15th	Topic #2 Written Reports Due & Chapter 11 Credit Selection, Underwriting & Portfolio Diversification & Case #13
Oct. 17th	Topic #2 Oral Presentations
Oct. 22nd	Chapter 12 Consumer Lending & Case #14
Oct. 24th	Guest Bankers & Case 15
Oct. 29th	Chapter 13 Financial Futures & Forwards: Hedging & Pricing & Case #16
Oct. 31st	Chapter 16 International Banking & Case #17
Nov. 5th	Bank Mergers and Acquisitions & Case #18
Nov. 7th	Topic #3 Written Reports Due, Strategic Planning for Future Performance & Case #19
Nov. 12th	Topic #3 Oral Presentations
Nov. 14th	Exam #3 (Chapters 11-13, 16, Mergers & Acquisitions, notes & lecture)
Nov. 19th	Directors Duties & Conduct of the Board Meeting & Case #20
Nov. 21st	Thanksgiving Holiday
Nov. 26th	Delivering Service Quality & Case #20
Nov. 28th	Barnett Pipe Co. Case (Presented by all groups)
Dec. 3rd	Marketing the Bank's Services
Dec. 5th	Comparative Bank Data Presentation
Dec. 12th	8:00 a.m. to 10:00 a.m. FINAL EXAMINATION All Previous Materials

Case Presentation Instructions
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The class will be divided into groups of three or four individuals to prepare and present three cases to the class. Two cases will be from the text and one will be **Barnett Pipe Co. Case** presented by all groups on November 28th.

The purpose of these group sessions is to develop a team solution approach similar to what would be encountered in the actual workplace. Grading for each of the cases will be based upon the following:

Analysis of the problem	1/3rd
Answers to the case questions	1/3rd
Oral presentation	1/3rd

The total grade for the cases will count 15% of their final course grade.

The due date for your cases is shown on the syllabus and must be turned-in on that date or a grade of “0” will be assigned for the case. **More than one person should be able to present the case in the unfortunate event that the presenter does not make it to class. Failure to turn-in and present the case will result in a grade of “0” for all team members.**

In preparing your cases for the class, they should be typed, double-spaced. They should state or analyze the problem presented, give a brief summary of the case and facts, and answer the questions presented with the case (**See How to Present Case Below**). Normally 15 minutes will be allowed for the oral presentation of each case. **The presentation should be in Power Point format and e-mailed to jbbexley@shsu.edu twenty-four hours before the case is due to be presented. It should be titled 468-Case#__.ppt (your case # goes in the blank.) For United Bank Case it should be titled 468cb-bb-group#__.ppt (your group # goes in the blank.)**

HOW TO PRESENT YOUR CASE SOLUTION

XYZ Bank Case #5
John Doe, Mary Smith, & Tom Adams

Case Description: In this area you should describe the subject matter for the case and any secondary issues that arise. As an example here is a sample case description for a case relating to a revolving line of credit-----*The primary subject matter for this case concerns the viability of making a revolving line of credit to an established company. Secondary issues involved in this case turn on analyzing credit issues such as evaluating ratios, evaluating strengths and weaknesses, proposing loan covenants, calculating eligible accounts receivable and inventory.*

Problems Presented in the Case: In this area you should address specific problems that you detect in the case. For example, in a case with credit quality issues you might see the following---*The case as presented shows a general weakness in the credit quality. Such items as the ratios are weak, earnings are not consistent, and there does not appear to be enough cash flow to pay existing debt as now structured.*

General Discussion of the Case: Here you should discuss the impact of risk, competition, profitability, or the other issues raised in the case. This should be approximately one page. For example, in a case with performance and risk issues you might see the following---

Competition

The banking industry is extremely competitive, and the profitability of the bank will depend primarily upon the bank's ability to compete in its market area. The bank competes with other commercial and savings banks, savings and loan associations, credit unions, finance companies, mutual funds, insurance companies, brokerage and investment banking firms, non-bank lenders and other non-financial institutions, including governmental organizations which may offer subsidized financing at lower rates than those offered by the bank. Simultaneously, consumers have more information regarding the terms offered by various service providers. This favors the low cost service providers, which may not be the traditional financial institution. The availability of traditional banking products from banks and non-banks on a national basis has put tremendous pressure on pricing margins.

SWBT has been able to compete effectively with other financial institutions by emphasizing technology and customer service, including local office decision-making on loans, establishing long-term customer relationships, building customer loyalty, and by providing customized products and services to its customers. The continued success of the company is dependent on the economic strength of the Houston metropolitan area.

SWBT will have to compete with financial institutions that have the ability to single source any financial product or service in a market area. The bank may discover that they lack adequate resources or efficiencies to compete against larger multinational or global banks and financial institutions. As a result, they may pursue acquisitions to further bolster or gain resources to improve efficiency in order to compete in an increasingly global financial market place.

Risks

The policies of regulatory authorities, including the monetary policy of the Federal Reserve Board, have a significant effect on the operating results of bank holding companies and their subsidiaries. Among the means available to the Federal Reserve Board to affect the money supply are open market operations in U.S. Government securities, changes in the discount rate on member bank borrowings, and changes in reserve requirements against member bank deposits. These means are used in varying combinations to influence overall growth and distribution of bank loans, investments and deposits, and their use may affect interest rates charged on loans or paid for deposits. Other risks faced by SWBT include unfavorable economic conditions in the Houston area. This could negatively impact the bank's customers, cause declines in the value of loan collateral, a reduction in loan demand, and an increase in loan losses.

SWBT follows a conservative approach to lending and credit relative to other Texas regional banks. Risk in terms of credit quality is minimal and is evidenced by a level allowance for loan losses to total loans over the last four years. Also, net charge-offs to average loans has declined over the same period. With a climate of lower interest rates, and the possibility of an economic rebound, the bank may be able to benefit from cheaper sources of available credit.

The bank has a current ratio of 1.08 and is well capitalized. Core deposits make up 83% of the total deposits and the loan to deposit ratio is 80.9%. Given the low credit risk, strong capitalization, and high amount of core deposits, liquidity risk is minimal.

Performance versus Peers

The bank's performance is comparable to other Houston area regional banks such as Compass, Sterling, Frost, Guaranty, and Woodforest. It competes favorably against the larger commercial banks such as Chase, Wells Fargo, and Bank America as measured by ROA, ROE, Net Interest Margin, Non Interest Expense, and Capital/Assets. In order for the bank to better compete and further differentiate itself from the other regional banks, SWBT can be more aggressive with its lending by slightly easing its credit standards given the amount of capital/assets and loans/deposits relative to the other regional banks. It can also be more competitive with the regional banks by broadening its menu of products and services to clients. Such efforts should focus on new services that generate fee-based income and diversify the bank's sources of revenue.

Solutions to Questions: Here you should list the question presented in the case and answer each question.

Term Paper Instructions
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As set out in your class schedules, there are three written topic times designated for turn-in and presentation. You will be assigned session #1, #2 or #3. Each student will make a written and an oral presentation at the time determined by the topic number. All topics must be turned-in by **August 27th**. If you have **Topic #1**, the turn-in date for the written research paper is **October 1st** and the day oral presentations will be made, is **October 8th**. Written research papers if you have **Topic #2** must be turned-in on **October 15th**, and oral presentations made on **October 17th**. If you have **Topic #3**, the turn-in date for the written research paper is **November 7th** and the day oral presentations will be made, is **November 12th**. Any paper turned-in late will receive a grade of F. Following-up on the oral instructions given you in class, this set of instructions will give you firm, written directions concerning the written and oral assignments.

1. The term papers should be written in good manuscript form, utilizing proper grammar, spelling and punctuation. The topics are to be pre-approved by the instructor.
2. Your paper should be double-spaced with a normal margin and be a minimum of **eight** typewritten pages and a maximum of **twelve** typewritten pages in 12 point times or times roman type font.
3. There must be a minimum of two research references, not including the FIN 468 text, and only one may be from the Internet.
4. On the date your research paper is due, you will turn-in your research paper in hard copy (paper), and you will e-mail your oral presentation to jbbexley@shsu.edu with a title of 468(Your Last Name).ppt and then you will deliver your oral presentation of the term paper to the class the assigned day **using Powerpoint**. The oral presentation will be no less than four minutes nor more than five minutes. This presentation should clearly and concisely present the concepts advanced in your written presentation.
5. As you know, the combination of the term paper and the oral presentation will count 20% of your total final grade.
6. The following topics will be utilized unless the professor approves another topic in advance:
 1. The Role of the Debit Card In the Bank of the Future.
 2. The Importance of Strategic Planning in the Bank's Performance.
 3. Risk Management As A Regulatory Tool.
 4. The Role of Consumer Lending In Banking.
 5. The Role of Commercial Lending In Banking.
 6. The Role of Mortgage Lending In Banking.
 7. Asset/Liability Management in the Bank.

8. The Future of Community Banking.
9. The Relationship of Management and the Board of Directors in the Bank.
10. The Impact of Sarbane-Oxley on Community Bank Governance.
11. The Changing Role of Marketing in Banking.
12. Advantages of the Bank Holding Company.
13. Differences Between Credit Unions and Commercial Banks.
14. Methods of Efficiently Generating Funds To Loan To Bank Customers.
15. The Role That Capital Plays in the Functioning of the Bank.
16. Why Have Bank Mergers Become So Attractive?
17. Market Research Methods/Techniques for Commercial Banks
18. The Benefits of Internships to Banks and Students
19. Credit Analysis and Its Role In The Commercial Loan Approval Process.
20. Using Focus Groups To Help Establish The Bank's Marketing Thrust.
21. The Importance of Customer Service In A Bank.
22. The Status of DeNovo Bank Chartering in the U.S.
23. Bank Expansion—Is Branching or Buying Best?
24. The Impact of Inflation On Bank Profits
25. The Effect of Corporate Paper on Commercial Banks
26. The Use of Unconventional Products In Banks
27. Fee Income's Impact On The "Bottom-line"
28. The Federal Reserve Bank's Role In Bank Holding Companies
29. State Non-Member Bank Regulation of Commercial Banks By The Federal Deposit Insurance Corporation and State Regulators
30. State Member Bank Regulation of Commercial Banks By The Federal Reserve Bank and State Regulators
31. National Bank Regulation of Commercial Banks By The Office of the Comptroller of the Currency
32. Has Credit Quality Diminished In Bank Lending?
33. The Future of the Dual Banking System In The U.S.
34. Is a Single Bank Regulator System Likely In The U.S.?
35. How Banks Can Achieve High Performance Banking
36. The Future of International Banking In a Global Economy
37. The Role of the Investment Portfolio in the Bank
38. Has the Repeal of the Glass-Steagall Act Hurt Community Banking
39. The Impact Basel Accord or Agreement Will Have on U. S. Bank Capital
40. The Impact of the USA Patriot Act on Banks
41. "Payday Lending" and Sub-prime Lending in Banking
42. The Role of Deposit Pricing and Loan Pricing in Bank Profitability
43. Comparing Judgmental Credit Practices to Credit Scoring Practices
44. The Universal Bank Model
45. Can Community Banks Compete with Investment Firms?
46. Enterprise Risk Management In Banks
47. Activity Based Cost Accounting for Banks
48. How Customers Perceive E-Commerce In Banking
49. How Banks Blend High Tech with High Touch
50. How Service Quality Impacts Banks

BARNETT PIPE COMPANY

By
James B. Bexley

CASE SYNOPSIS

The case focuses on a Columbus, Ohio company that was started fifteen years ago. This company is unique in several ways. First, it provides hard plastic gas lines to contractors who install these lines for municipalities. Second, it is unique in that national and regional building codes have mandated the installation of hard plastic gas lines to replace the steel pipe lines used for many years. Students are expected to closely examine the company's financials over a four-year period, and evaluate and discuss such issues as the company's liquidity, financial options, sales trends, and receivables collection. Another unique issue is the interest rate risk caused by a fixed rate loan and how to mitigate the risk issue.

INTRODUCTION

The Barnett Pipe Company is located in Columbus, Ohio. They have been in operation for 15 years. They are a company that specializes in the manufacturing of hard plastic lines utilized to transmit natural gas to residential and commercial users. There are various diameters of piping and connectors that link to comprise a reliable and serviceable gas system.

Originally, natural gas was transmitted through steel gas lines, however, in the last ten years, most national and regional building codes specify transmission through high-test hard plastic gas lines. In Columbus, the city has mandated by code that new residential gas lines use pressure-tested plastic. The current metal infrastructure is being slowly replaced in Columbus and surrounding areas.

Barnett Pipe Company is a medium sized company with a great reputation for service and quality products. Every roll of gas pipe is independently tested twice before leaving the shop. They also provide their customers with the equipment and encourage them to perform another test before installation. This redundancy in testing drastically reduces the possibility of gas line failure and thus reduces the potential for litigation against the company.

MARKET ANALYSIS

There are four major contractors that are certified to the install gas lines in the greater Columbus market. The two largest obtain their pipe from Barnett Pipe Company. The other two both obtain their piping from Texas Gas Supply Corporation, another gas line manufacturing company located in Houston, Texas. One of the companies has indicated that they would like to use Barnett Pipe Company to supply them but they have a year left on their contract with Texas Gas Supply. Barnett Pipe feels strongly that they will get this contract at the termination of the contract with Texas Gas Supply. Prices for Barnett Pipe Company's products tend to be slightly higher than Texas Gas Supply, but Texas Gas Supply is much slower in their responses to problems and they don't have the support staff to service their contractors as well. Barnett Pipe has also been selling to cities in the state of Texas for the past five years with good success. These areas are closer to the main competition, but this has not impacted Barnett's ability to continue to build market share in its main competitor's state.

BANK RELATIONSHIP

Barnett Pipe Company has been banking with Ohio National Bank (ONB) for 5 years. They have a \$570,000 revolving line of credit with ONB to purchase raw materials for their production. They have always kept their loan in good standing. They have never had a late payment but there were two occasions in which their payments were below a negotiated amount. They did make amends in the very next month following these incidents.

Table 1
Bank Relationship

Credit Record	High	Low
2003	556,500	194,775
2004	500,850	55,650
2005	445,200	0
2006	556,500	139,125

LOAN REQUEST

Their current loan request is for \$90,000. This loan will be for the renovation and reorganization of two of their warehouses and the purchase of 4 new, heavy-duty forklifts. Barnett Pipe Company currently owns and operates 7 forklifts. Four have been used since the company began 15 years ago and the other three were purchased 7 years ago. The original 4 have been rebuilt twice already and are in poor shape currently. The time and effort spent servicing have made these four counter-productive and are costing the firm more than they are worth. The new units will be roughly \$5,000 apiece. The remainder of the loan will go towards the renovation and the reorganization of the warehouses.

The company has requested a four-year term loan that would be paid back in 48 equal monthly payments. Frank Lawrence a Senior Vice President at ONB has been Barnett's loan officer for the past ten years. He is presenting to the loan committee at ONB a term-loan of \$90,000 over a period of four years at a fixed interest rate of 6.8%

and repayable in even payments over a 48 month period. At this time ONB's prime-rate is 6.0%.

FINANCIAL INFORMATION

Barnett has provided the following financial information for the bank's use in evaluating a loan request:

Table 2
South-West Pipe Company Balance Sheet 12/31/2003 - 12/31/2006

Assets	2003	2004	2005	2006
Cash	303,849	77,910	35,616	27,825
PrePaid & Deferred Expenses	30,051	11,130	10,017	54,537
Fixed Assets Net of Depreciation	270,459	253,764	414,036	459,669
Accounts Receivable Net	601,020	684,495	422,940	513,093
Other Receivables	0	0	0	83,475
Inventory	1,003,926	1,021,734	1,266,594	1,040,655
Total Assets	2,209,305	2,049,033	2,149,203	2,179,254

Liabilities	2003	2004	2005	2006
Notes Payable	500,850	445,200	356,160	406,245
Current Maturities of Term Debt	0	0	34,503	34,503
Long Term Debt	0	0	159,159	317,205
Accrued Expenses	156,933	104,622	211,470	124,656
Accounts Payable	625,506	683,382	648,879	614,376
Capital Stock	445,200	445,200	445,200	445,200
Retained Earnings	480,816	370,629	293,832	237,069
Total Liabilities	2,209,305	2,049,033	2,149,203	2,179,254

Table 3
South-West Pipe Company Income Statement 12/31/2003 - 12/31/2006

	2003	2004	2005	2006
Net Sales	8,020,278	7,917,882	7,547,253	6,811,560
Cost of Sales	6,517,728	6,531,084	6,233,913	5,540,514
Gross Profit	1,502,550	1,386,798	1,313,340	1,271,046
Total Operating Expenses	1,184,232	1,129,695	1,085,175	987,231
Operating Profit	318,318	257,103	228,165	283,815
Income Taxes	152,481	124,656	115,752	136,899
Net Profit	165,837	132,447	112,413	146,916
Depreciation	48,972	51,198	52,311	58,989
Dividends Paid	55,650	55,650	55,650	0

Table 4
Relevant Assets

Inventory	Current	Percent
Raw Material & Supplies	417,375	41.5
Work in Progress	241,521	24.1
Finished Goods	345,030	34.4
Totals	1,003,926	100.0

Receivables (Aged as Follows)	Prior	Percent
Current	513,093	85.3
30 - 60 Days	35,616	5.9
61 - 90 Days	17,808	3.0
91 Days and Over	34,503	5.8
Totals	601,020	100.0

ANALYSIS

Your job as a credit analyst for the Ohio National Bank is to answer the following questions in order that Mr. Lawrence will be prepared to make a presentation to the bank's loan committee.

1. Review the financial data attached in Tables 1 through 4 and discuss the company's liquidity.
2. Why doesn't Barnett Pipe Company pay for these upgrades through their existing line of credit?
3. Look at the trends in sales for the past four years. Will the company be able to generate enough in sales to repay the loan?
4. Analyze the relevant assets in exhibit 4. How important is the company's ability to collect from its debtors towards the final decision for the loan?
5. Does the rate proposed by Mr. Lawrence of 6.8% fixed pose any interest rate risk sensitivity issues for the bank?
6. If the rate of 6.8% does pose an interest rate risk sensitivity issue, what options are available to the bank to mitigate the issue?

HANDOUTS
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