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The road ahead narrows for Capitol Bancorp

By Lindsey White

After dropping its rights offering Feb. 23, Capitol Bancorp Ltd.'s options to raise much-needed capital appear limited.

The Lansing, Mich.-based bank raised $7.5 million in capital in April 2010, but decided to try to raise funds again through a rights offering less than a year later after successive quarterly losses continued to eat into the company's capital levels.

However, a little more than a month after filing for the rights offering, Capitol Bancorp withdrew the transaction. That same day, shareholders approved proposals to increase the number of authorized shares of capital stock to 1.52 billion from 70 million, and to effect a reverse stock split. Capitol Bancorp also said it may undertake a subsequent private offering.

With the company's stock trading at 15 cents a share Feb. 25, any capital raise would be tough for the company, said John Donnelly, a managing director of Donnelly Penman & Partners. "I don't think it's being traded on any type of valuation fundamentals [like] book value or earnings," he told SNL Financial. "I think when a stock gets down to these prices, it's trading on speculation about whether or not it's going to survive."

In this situation, Donnelly said the company's options are limited. "I think the only option left for capital is to continue the program that they're on, [which] is to try to sell the parts," Donnelly said.

Capitol Bancorp has entered into agreements to sell close to 20 of its subsidiary banks to bolster its capital levels and shrink its balance sheet. The moves have come in response to several enforcement actions issued at the bank level and a written agreement entered into with the Federal Reserve in September 2009. Donnelly said this is a viable strategy that has been successful for the bank thus far. "But ultimately the regulators hold the trump cards," he said. "Hopefully the regulator will allow them enough time."

Capitol Bancorp Director of Communications Angela Kimber declined to comment until after the company has released its year-end results.

How much time a bank has to repair its balance sheet depends on the plan the institution has in place to raise capital. Before closing a bank, regulators generally consider a bank's capital restoration plan to determine if it is based on realistic assumptions, said John Geiringer, a partner at Barack Ferrazzano Kirschbaum & Nagelberg LLP who has worked with the FDIC's resolution team. One important factor is whether regulators believe that the bank will achieve "adequately capitalized" status — a leverage ratio of 4% or greater — within a reasonable period of time.

"Part of it will depend on how far down you are," he said. "If you're just below 'adequately capitalized,' they may give you more time than if you're way far down," he told SNL. Regulators will also take factors like a bank's level of classified assets into consideration, Geiringer said.

If a bank is "critically undercapitalized," however, Geiringer said regulators' discretion is limited.

Banks are deemed "critically undercapitalized" when their Tier 1 leverage ratio drops to 2% or less. As of Dec. 31, 2010, Capitol Bancorp has a Tier 1 leverage ratio of negative 1.03%, according to SNL Financial data compiled from the institution's call report.

A Texas ratio in excess of 100% is widely regarded as the threshold at which banks tend to fail. As of Dec. 31, 2010, Capitol Bancorp had a Texas ratio of 570.91%.

"They should sell what they can sell," Donnelly said. "The boat is taking on water — they've got to throw some stuff overboard."