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VIEWPOINTS

It's a Good Time for Issuer Tender Offers



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Bank and thrift stocks, including mutual holding companies, have dropped dramatically since January 1, 2007, because of the challenging interest rate environment and concerns about credit quality, and yet community banks are generally well capitalized and profitable.

This environment provides many banks with the opportunity to enhance their franchise value and please shareholders through an issuer tender offer — a public offer by a company to repurchase its own securities (typically common stock) from shareholders at a premium to the current market price.

A prime advantage of a tender offer is that an issuer can contact all shareholders with the terms and thus increase the likelihood that a significant number of shares will be repurchased. The offers are generally accretive to earnings (and possibly book value) when bank stocks are depressed, and shareholders benefit from the added liquidity by selling at a price equal to or above the prevailing market price.

Issuer tender offers are proactive, unlike the more familiar stock repurchase programs, which are typically passive in nature

and generally depend on shares being bought at the market price in the open market or in private transactions.

Depending on the stock's trading price, an issuer tender offer provides an opportunity for the company to repurchase a significant number of shares at an attractive price — close to its book value per share, near the initial public offering price, or below the recent trading range. Though other capital management strategies such as paying a special dividend can help the stock price in the short term, the impact is diminished after the ex-dividend date.

Alternatively, under the right circumstances a tender offer can improve a company's balance sheet and income statement.

Over the past year stock prices have dropped for a significant number of recently converted institutions (including mutual holding companies that completed second-step transactions). For such institutions, an issuer tender offer is almost always accretive to earnings and may be accretive to book value. Thus, for both recently converted (past the one-year anniversary of their conversion) and seasoned companies, an issuer tender offer is an effective capital management tool, as it helps strengthen the company, because it can reduce the outstanding shares, resulting in enhanced earnings per share, while deploying excess capital.

For companies with low trading volume, an issuer tender offer gives shareholders an opportunity to sell their shares without driving down the market price. Because the company is the ready buyer, larger transactions can be made than would occur in the open market.

Issuer tender offers typically are made at a premium of up to 10% of the pre-announcement market price, so there is a greater likelihood of success. For mature companies, the pricing will be closer to the historical average for a peer group of institutions but

can result in an improved return on equity.

Financial institutions that may consider a sale in the future also should be interested in issuer tender offers, as a successful one will position the company to obtain a higher price per share for the remaining shareholders.

Finally, a tender offer lets a company buy out indifferent or hostile shareholders, thereby resulting in a more company-friendly investor base.

An issuer tender offer is a bit more complex than a stock repurchase program. The company must decide whether to offer one price or a range of prices in a modified Dutch auction, in which shareholders select the price where they would be willing to sell. In addition, a tender offer is subject to SEC rules that the same terms, including price, are offered to all shareholders; that shareholders have a right to withdraw their tenders while the offer remains open; that it remains open for at least 20 business days; and that the company must repurchase the shares on a pro rata basis if the offer is oversubscribed.

It takes approximately three months for an issuer tender offer to complete. Once the board of directors decides to commence an offer, the documents and schedules for filing with the SEC are prepared, and an investment banker is hired to assist the board in recommending pricing levels.

The offer commences (and materials are mailed to shareholders) at the same time the documents and schedules are filed with the SEC. While the SEC may comment on the offer materials, this usually does not lead to mailing revised materials to shareholders.

Once the offer is completed, preliminary results are disclosed, and the purchase of shares is completed within five to seven trading days.

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