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Santander feels pressure of Fed's stress tests

MARK LENNIHAN/ASSOCIATED PRESS/FILE

Banking consultants say Santander is solvent, but has some work to do.

By **Deirdre Fernandes** GLOBE STAFF MARCH 21, 2015

Boston-based Santander Holdings USA Inc. earned the dubious distinction last week of being the only large bank to fail the same portion of the Federal Reserve's annual checkup for two years in a row.

Federal regulators said the bank had a healthy amount of money, but criticized it for "widespread and critical deficiencies" in its management and planning, raising questions about how the bank would prepare for a severe recession. It's a bit like having a doctor tell a patient he is in good health and can survive most illnesses, but faces problems down the road if he doesn't pay attention to risks like cholesterol and blood pressure.

Bank consultants, analysts, and former regulators said that Santander, which is owned by the Spanish banking giant Banco Santander SA, is financially sound and solvent. But failing the Fed's stress tests twice, because regulators don't trust how the bank manages risk, could keep Santander from pursuing its larger ambitions to expand in the United States.

Pat Rohan, a managing director for New Jersey-based FinPro Inc., a bank consulting firm, said Santander will have to spend plenty of money to fix its management practices to satisfy the Fed. "It's very expensive and very time consuming," he said.

It can also raise concerns for depositors. The state's treasurer, Deborah Goldberg, and her senior staff members met with Santander executives Wednesday to discuss the Fed test and receive assurances the bank was fixing the problems, said Matt Sheaff, a spokesman for the treasurer's office.

Massachusetts has $592 million in 376 accounts at Santander, which guarantees the deposits. "We will continue to receive updates from Santander on their progress as they address the qualitative concerns raised by the Federal Reserve," Sheaff said.

Santander, the third-largest bank in Massachusetts, became a major presence in the US market in 2009 when it purchased Sovereign Bank. Its US operations earned $1.3 billion in 2014, according to regulatory filings.

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Santander officials said their focus in the United States is not making acquisitions and expanding the bank's footprint, but building the existing business and "meeting regulatory expectations." In recent months, Santander has made management changes to address some of the Fed's concerns and it is promising more.

The Spanish bank earlier this month hired a separate chief executive for its US holding company, a title that had also been held by the bank president, Roman Blanco. The holding company's new executive officer, Scott Powell, was not available for comment.

Santander also has also improved its technology and data management, a spokesman said.

Those changes weren't enough for the Fed, which began administering its "stress" tests following the 2008 financial crisis to avoid future taxpayer bailouts of big banks. The banks are given scenarios where unemployment spikes and the real estate market tanks to determine how well their loans and businesses would perform. The tests also examine if bank executives are aware of and could manage underlying risks.

Banks overall have significantly improved their capital cushions to absorb losses in a severe crisis since the tests began in 2009. And many banks have spent millions to focus on the second part of the Fed's evaluation, which is on how well an institution plans for the worst-case scenario.

To pass muster, banks have hired workers and updated technology to analyze risks, ensured that loans aren't concentrated in one industry, and dumped certain risky lines of business. Citigroup Inc., for example, failed the second round of the stress tests last year, but passed this year. It recently said it would sell OneMain Financial, a subprime lender that has been under greater regulatory scrutiny.

The Fed does not disclose the specific problems it finds at banks. In Santander's case, the regulators lumped their concerns into broad categories, such as governance, internal controls, and risk management.

The Fed does give the banks very detailed information about the problems, bank consultants said. "Every bank, by the time they've talked to regulators, they know what to do," said Kamal Mustafa, chief executive of the Invictus Consulting Group, a New York-based bank advisory firm.

That's why it will be important for Santander, a large, global institution, with plenty of resources, to get this right next year, banking consultants said. "They're a big enough organization they should have the resources to address it," Rohan said.

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