

June 17, 2009

**Research Update:**

# First National Bank of Omaha 'BBB-' Rating Affirmed, Off Watch; Outlook Negative

**Primary Credit Analyst:**

Jeffrey Zaun, New York (1) 212-438-2739; jeffrey\_z aun@standardandpoors.com

**Secondary Credit Analyst:**

Daniel E Teclaw, New York (1) 212-438-8716; daniel\_t eclaw@standardandpoors.com

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## Research Update:

# First National Bank of Omaha 'BBB-' Rating Affirmed, Off Watch; Outlook Negative

## Overview

- Management at First National of Nebraska Inc., the parent of First National Bank of Omaha, has cut expenses and maintained asset quality that we feel is better than peers'.
- We are removing First National Bank of Omaha from CreditWatch and assigning a negative outlook.
- Despite good funding and some improvement in preprovision earnings, First Nebraska's weak capital provides scant cushion against any increase in credit losses.

## Rating Action

On June 17, 2009, Standard & Poor's Ratings Services affirmed its 'BBB-' long-term counterparty credit rating on First National Bank of Omaha, a subsidiary of First National of Nebraska, and removed it from CreditWatch Negative, where it was placed May 4, 2009. The outlook is negative.

## Rationale

The affirmation balances our view that the recession could drive deterioration in credit quality and profit against First Nebraska's good core deposit funding profile, its location in areas where this business cycle has been muted, and its better-than-average asset quality. The affirmation and outlook change follow an ongoing industry review and our recent criteria on stress testing and U.S. banks. We are concerned with the firm's weak earnings, weak capital, and concentration in credit-card lending (31% of the managed portfolio) and commercial real estate (CRE; 20% of the portfolio).

Although the bank has contained credit losses, its high credit risk profile and soft core earnings render it vulnerable to losses that would worsen capital levels that are already weak relative to peers'--and very low given its exposure to higher-risk credit card and CRE loans. The outlook change is consistent with our reassessment of U.S. bank industry risk. Specifically, we believe that the banking system's credit outlook will continue to weaken and that economic activity will remain tepid. At the same time the housing and manufacturing sectors will continue to decline, along with household wealth. The resulting slowdown in consumer spending will hurt First Nebraska's earnings. We balance these risk factors against First Nebraska's strong deposit funding, diverse earnings streams, improved efficiency, and credit-card loss metrics that have been strong relative to other issuers'.

## Outlook

The negative outlook incorporates our view that credit quality metrics will likely deteriorate in a very difficult economic environment. To maintain its capital levels, management has cut costs, cut its dividend, raised prices, and reduced lending. Nevertheless, it may be difficult to improve profitability or prevent credit losses in the current weak environment.

We could downgrade First Nebraska if asset-quality trends indicate that losses will weaken capital levels. An upgrade is unlikely in the current environment. When economic conditions improve, we could revise the outlook to stable if profitability and capital levels strengthen.

## Related Research

- "Credit Stress Testing For Financial Institutions," published April 29, 2009.
- "Stress Testing U.S. Financial Institutions," published April 29, 2009.
- "What Stress Tests Reveal about U.S. Banks' Capital Needs," published May 1, 2009.

## Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
First National Bank of Omaha		
Counterparty Credit Rating	BBB-/Negative/--	BBB-/Watch Neg/--
Subordinated	BB+	BB+/Watch Neg

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