

June 17, 2009

Research Update:

Webster Financial Corp. Rating Lowered To 'BBB-'; Outlook Negative

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Research Update:

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Overview

- We increased our assumptions about industry loan losses, given the severity of the national recession.
- We are downgrading Webster Financial Corp. to 'BBB-'.
- We expect the recession to continue to put pressure on Webster's capital and profitability.

Rating Action

On June 17, 2009, Standard & Poor's Ratings Services lowered its long-term counterparty credit rating on Webster Financial Corp. (Webster) to 'BBB-' from 'BBB'. We also lowered our counterparty credit rating on Webster's main bank subsidiary, Webster Bank N.A. to 'BBB/A-2' from 'BBB+/A-2'. We removed all ratings from CreditWatch Negative where they were placed May 4, 2009. The outlooks are negative.

Rationale

The rating action follows our recent U.S. banking industry review, in which we reevaluated our expectations for industry loan losses. The downgrade reflects Webster Financial Corp.'s asset-quality deterioration to-date and our expectation that nonperforming assets (NPAs) will continue to rise in the severe recession. Asset-quality deterioration may cause additional pressures on Webster's below-average profitability and tangible common capital levels, in our view.

With about \$17 billion in assets, Webster is a midsize Connecticut-based bank with decent market positions in its home counties. Its most prevalent asset-quality issues have been in previously identified home equity and out-of-footprint residential construction "liquidating" portfolios. Another weak portfolio, in our view, is its \$156 million residential development portfolio. Positively, these portfolios represented less than 4% of loans as of March 31, 2009. Still, there are signs of asset-quality deterioration in other loan types, such as its commercial loan portfolios, because of the economic downturn. Although we recognize that Webster's southern New England market has held up better than have more distressed areas in the country, we factor in the likelihood of a further moderate regional economic decline.

The NPA ratio was about on par with peers' at 2.87% as of March 31, 2009, but it rose from 2.15% at the prior quarter-end. The net charge-off rate, while reduced to 0.99% in the first quarter, has been volatile on a quarterly basis, illustrated by the very high 1.66% net charge-off rate in fourth-quarter 2008.

Webster has reported recent quarterly net losses, largely from loan-loss

provisions, although its net loss narrowed to \$22 million (available to common shareholders) in first-quarter 2009. We believe there is a high probability that Webster may report a net loss in 2009, reflecting continued high loan-loss provisions. In addition, it may take further losses in its trust-preferred investment portfolio, although much of this portfolio has already been written down. Webster's core earnings power is not strong, in our opinion, because of its reliance on spread income, the recent decline of its net interest margin, and its high expense base.

The rating takes into account the buffer of Webster's strong regulatory capital levels, which are bolstered by a large proportion of preferred stock. However, a less favorable capital measure is Webster's modest tangible common equity (TCE) ratio of 4.05% as of March 31, 2009. Positively, management is focused on building the TCE portion of its capital base.

For example, in late May 2009, the company announced an offer to exchange for common shares \$168.5 million of convertible preferred and \$200 million of trust preferred stock. Even if partly successful, the exchange would likely improve the TCE ratio significantly, and this development would support the ratings. However, we believe Webster's TCE will still be somewhat below that of peers, and not particularly strong relative to balance-sheet risk.

Outlook

The negative outlook addresses uncertainties about the severity of the decline in asset quality, profitability, and capital trends. Current ratings anticipate a moderate rise in NPAs and the potential for a modest net loss in 2009. We could lower the ratings if NPAs rise more than we currently expect or if the company reports substantial net losses that significantly harm capital ratios. Conversely, we could revise the outlook to stable if asset quality stabilizes and the company returns to more normalized earnings levels on a sustainable basis.

Related Research

- "Credit Stress Testing For Financial Institutions," April 29, 2009
- "Methodology And Assumptions: Risk-Adjusted Capital Framework For Financial Institutions," April 21, 2009
- "Stress Testing U.S. Financial Institutions," April 29, 2009

Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Webster Financial Corp.		
Counterparty Credit Rating	BBB-/Negative/--	BBB/Watch Neg/--
Senior Unsecured	BBB-	BBB/Watch Neg
Preferred Stock	B+	BB-/Watch Neg
Webster Bank N.A.		
Counterparty Credit Rating	BBB/Negative/A-2	BBB+/Watch Neg/A-2
Certificate Of Deposit		

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Local Currency Subordinated	BBB/A-2 BBB-	BBB+/Watch Neg/A-2 BBB/Watch Neg
Webster Capital Trust IV Preferred Stock	B+	BB-/Watch Neg
Webster Preferred Capital Corp Preferred Stock	BB-	BB/Watch Neg

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