



# NEWS RELEASE

FOR IMMEDIATE RELEASE: December 6, 2011

## **Banking & Economic Forecast 2012**

By Chris Martin

Chairman, President and Chief Executive Officer  
The Provident Bank

With continued economic uncertainty, banks made front page headlines this year. From ongoing challenges in the housing market and the international debt crisis, to the stream of regulations and the recent “Occupy Wall Street” movement, there wasn’t a dull moment in banking in 2011.

When combined with persistent unemployment, these events will impact the banking industry and overall pace of the economic recovery in 2012. Though we are seeing the lowest rates in history, consumer confidence remains largely unchanged from last year. Lack of faith in the ability of our elected officials to get things accomplished has also added to the uncertainty.

While our European counterparts continue to struggle, many U.S. banks are well-capitalized and profitable. In New Jersey, for example, the great majority of banks are strong. In fact, four community banks have ranked in the top 50 among larger, national institutions. As a result, many have increased their lending to viable, creditworthy businesses.

However, the reality is the economic recovery is plodding. Home values – most Americans’ biggest asset – are depressed. According to a recent survey by the Mortgage Bankers Association, more than 100,000 homeowners in New Jersey are dealing with foreclosures that are stalled in the courts, while another 48,000 are way behind on payments. We can expect ongoing weakness in the housing market through mid-2012.

### *Coming Changes*

From a regulatory perspective, the world has changed completely. Additional oversight in the financial services industry has already begun. The Dodd-Frank Act, and the creation of the Consumer Financial Protection Bureau, will result in increased costs of compliance. Some banks had no alternative but to hire additional staff to handle these issues, and the expenses associated with these additional regulations will ultimately be passed on to consumers and businesses.

The Federal Reserve is likely to keep short-term interest rates near zero until mid-2013. In downgrading its outlook for the economy, the Federal Reserve predicted growth of no more than 2.7 percent in 2012, well below what is needed to lower the unemployment rate which is stuck at historically high levels.

In New Jersey, Governor Christie has approved a number of pro-business policies, including reducing corporate taxes, cutting bureaucratic red tape, extending tax incentives to prevent private-sector layoffs and privatizing state resources like concessions in parks. He has also increased the R&D tax credit from 50 percent to 100 percent by January 2012.

### *Challenges*

As interest rates continue to fall in the midst of already-low CD rates and savings yields, it's getting more difficult for those living on a fixed income to depend on interest from CDs as a main source. The days where you could ladder CDs and keep up with inflation are over.

The record high government spending has been felt by all Americans. It has created structural deficits of historic proportions which strengthen the likelihood of another credit downgrade by rating agencies of U.S. debt. The super committee of Congress failed to reach an agreement on measures that would reduce debt by \$1.2 trillion over the next decade, which spawns even more challenges for a slowly improving economy.

Consumer spending will be affected if the soon-to-expire payroll tax cuts and extensions in unemployment benefits are not renewed. And, the Bush tax cuts are set to expire at the end of 2012. Congress may preserve the cuts to consumers in the lower- and middle-income brackets, while the top income brackets could see a return to 39.6 percent compared to today's 35 percent.

Given the difficult economic environment, some consumers and small businesses remain uncertain about their individual financial health. Concerns about the stock market, the costs of food and gas, as well as fiscal policies will ultimately impact spending, a key driver of economic growth.

### *Trends*

The national movement to switch to community banks and credit unions has gained momentum. Following the recent debit card fee scares and the reverberation from movements like "Occupy Wall Street" and "Bank Transfer Day," we are seeing people migrate away from the larger banks to small or mid-sized financial institutions they feel they can trust.

Unlike the beginning of the recession when consumers pulled back the reins on spending – and increased their savings to as high as 8.3 percent – consumers financed their spending sprees in 2011 by sharply reducing their savings. According to data from the Department of Commerce, the savings rate is near its lowest level since the beginning of the recession, around 3.5 percent. Consumers seem to be spending more as evidenced by Black Friday sales, which reported a record \$52.4 billion, a 16 percent increase over last year.

The savings rate should be higher, particularly since baby boomers are living longer. However, amid a shaky economy, many are putting off retirement. Workplace retirement plans, personal investments or real estate losses have convinced many they won't be able to live comfortably. People are looking for sound financial advice to help maintain their standard of living. To help meet these demands, Provident expanded its wealth management capability with its recent acquisition of Beacon Trust Company.

Another trend lies in mortgage refinancings which are still in demand. Households have taken a big hit since the beginning of the recession, but we are seeing more households use their income to pay off existing debt. Mortgage rates have continued to drop, and recently fell below 4 percent again. However, borrowing costs have done little to spur home sales, which have remained unchanged and will continue to lag in 2012.

### *Good News*

While many New Jersey businesses may be reluctant to hire, some have reported a second year of improved sales, profits, spending and employment. This is a slow, but steady improvement, and we can expect businesses to proceed with caution in 2012.

But overall, many businesses are in good financial shape and can take advantage of new opportunities. When provided with the right financial guidance for handling pending increases in health care and regulatory costs, more businesses should be in a position to grow and hire more employees.

For instance, we are seeing a lot of activity with Small Business Administration (SBA) loans. The high unemployment rate has spurred a new pool of entrepreneurs and start-up companies. Provident's SBA loans are up 50 percent over the last year, so we anticipate continued demand. Businesses also benefit from our Preferred Lender status which gives us the authority to approve loans directly.

New Jersey's real estate sector is slowly recovering from the recession, and should continue to see steady progress in the years ahead. The Northeast is one of the strongest commercial real estate markets in the country. The retail vacancy rate is about 8 percent in New Jersey, compared to 12-15 percent nationally.

The multifamily market, in particular, continues to be the most desirable from a lending standpoint. The steady cash flow resulting from stable rent and occupancy levels is more attractive in comparison to other real estate properties.

The pace of improvement is much less than we all desire, but we are going in the right direction. Despite the uncertain economy, Provident remains well capitalized as defined by regulators. In 2012, our strong capital base will support our growth plans and provide stability for our ongoing lending operations. I am proud to be the CEO guiding Provident, as we continue to help our customers meet their financial goals.

### **About The Provident Bank**

With \$5 billion in deposits, The Provident Bank ([www.ProvidentNJ.com](http://www.ProvidentNJ.com)) serves its customers via a network of more than 80 branches throughout northern and central New Jersey. The Provident Bank is the wholly owned subsidiary of Provident Financial Services, Inc. (NYSE:PFS), which reported assets of \$7 billion as of September 30, 2011.

###