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This 3DAdvisors Report Covers:	
✓	**Insider Trading**: Insider Trading Behavior
✓	**Accounting**: Quality of Earnings Issues
	Governance: Corporate Governance Issues
✓	**Fundamentals:** Analysis of fundamentals
	Deception: Deception detection analysis

Executive Closest to Loan Exposures Sells Off Shares People's United Financial Inc. (NASDAQ:PBCT) Update

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Business Description

People's United Financial Inc. (PBCT) operates as the savings and loan holding company of People's United Bank that provides various financial services to individual, corporate, and municipal customers principally in Connecticut, Massachusetts, Vermont, New Hampshire, Maine, and New York. On January 1, 2008, People's United Financial completed its acquisition of Chittenden Corporation, a multi-bank holding company headquartered in Burlington, Vermont. As of 09/30/08, PBCT had total deposits of $14.2 billion. Its services include extending secured and unsecured commercial and consumer loans, and originating mortgage loans secured by residential and commercial properties, as well as accepting consumer, commercial, and municipal deposits. The Company was founded in 1842 and is headquartered in Bridgeport, Connecticut.

Summary of 3DAdvisors Findings for PBCT

- **Fundamentals:** Non-performing assets surge 50% sequentially
- **Accounting:** Non-performing assets jump, but reserves and charge-offs stay low
- **Insider Trading:** Commercial group chief and spouse drop almost entire stake

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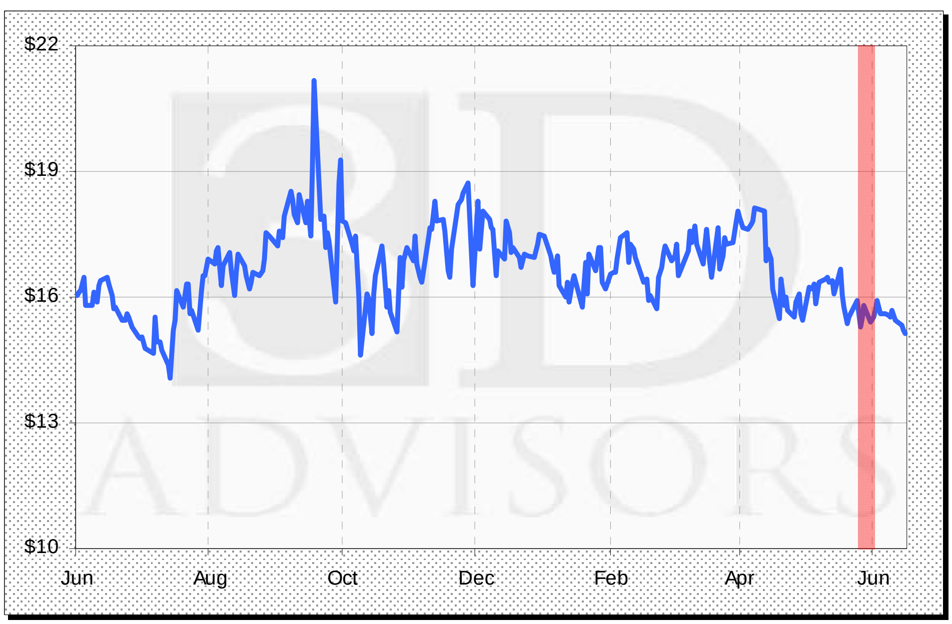
Discussion of 3DAdvisors Findings for PBCT

Since we covered People's United Financial Inc. (PBCT) in an issue of *Insider Research Bulletin* back on 11/18/08, the trading profile has captured our attention not only due its unusual and aggressive nature, but also because it stood in stark contrast to management's very bullish presentations and the lofty expectations of sell-side analysts. On the surface, management and analyst exuberance seemed justified; PBCT enjoyed an abundance of excess capital, little to no exposure to sub-prime residential mortgages, and exceptionally low allowances for loan losses and net charge-offs. Moreover, it had recently completed the acquisition of Chittenden Corporation of Burlington, VT, which significantly expanded its commercial loan portfolio and footprint into Northern New England. All in all, it appeared as if PBCT had an unusually strong balance sheet, was conservatively managed and poised to grow rapidly once an economic recovery began.

In our full report on 01/16/09, we suggested a possible explanation for the extreme disconnect between management's bearish trading profile and its bullish presentations and outlook. Namely, that PBCT had not entirely escaped the effects of a rapidly decelerating regional economy and that there were some exposures that were just beginning to manifest themselves, which may have been prompting insiders to head for the exits. More specifically, we wondered about the exposure in the commercial real estate portfolio, which represents the largest category of loans at nearly 35% of its total loan portfolio. We were particularly curious about exposures that might be lurking in the Shared National Credits portfolio, which was intended to give its loan portfolio geographic diversity but gave it exposure to more economically challenged areas of the country such as Florida, and the commercial portfolio that came along in the Chittenden acquisition, whose focus on commercial real estate lending in more rural Northern New England seemed to suggest greater potential risk, especially in an economic down turn. Commercial real estate loans stood at $2.2 billion and accounted for approximately 40% of Chittenden's total loan portfolio in its last filed SEC Form 10-Q (period ended 09/30/08) before the merger with PBCT.

Despite the persistent hyping of CEO **Philip Sherringham**, PBCT shares have more or less moved sideways since our full report in January. In the meantime, the storm clouds have been gathering, reported widely by the financial media, regarding the coming catastrophe commercial real estate portfolios at small and mid-sized banks are expected to suffer as the economy remains weak and commercial borrowers struggle to make principle and interest payments. Interestingly, the PBCT results for the 1Q09 (released 04/17/09) were once again dominated by much management bluster, but there were more pronounced hints of deterioration in certain areas, accompanied by somewhat obvious efforts to obfuscate the deterioration in the ensuing conference call.

Figure 1. PBCT Daily Closing Price, 06/02/08 to 06/16/09. Red shaded area is where Senior EVP Brian Dreyer sold 53,333 shares. Source: Reuters and PBCT SEC Filings.



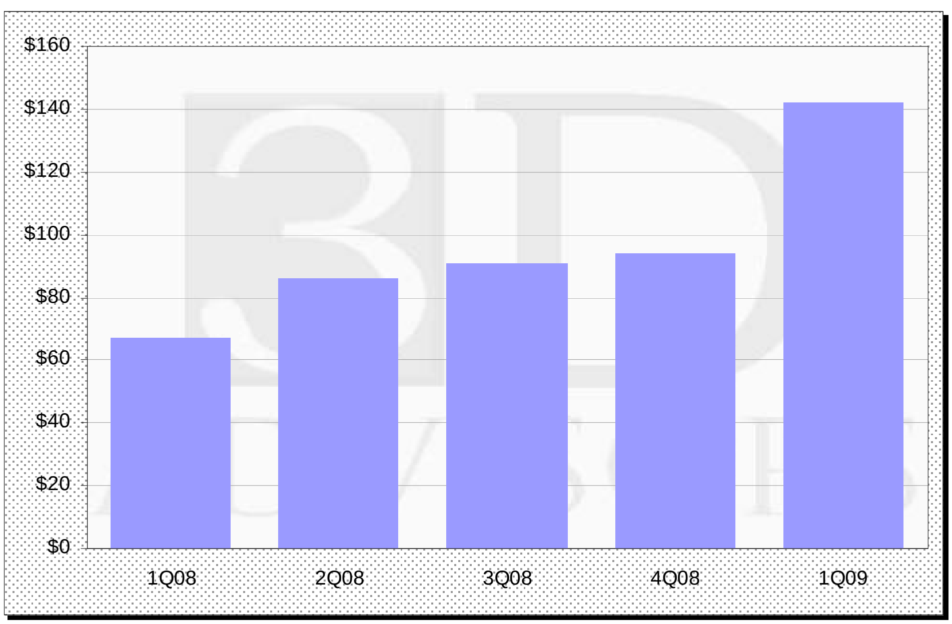
While all of the above is extremely interesting to us and more than enough to keep us focused on the name, it is once again the behavior of insiders at PBCT that has prompted us to issue this update. Between May 27th and June 1st, Senior EVP of the Commercial Banking Group **Brian Dreyer** sold 53,333 shares, representing the majority of his actionable holdings. We covered other dispositions by this key insider in our earlier reports on the Company, but what stands out to us in this instance is that he is lopping off a big chunk of his holdings at 15% lower prices than when he last sold in the 4Q08. We begin this update with a brief overview of the items that stood out to us in the 1Q09 results and conference call.

Fundamentals: Non-performing assets surge 50% sequentially

Even though the 1Q09 conference call was once again replete with assertions by management that PBCT is in far better shape than its banking brethren, there were clearly some cracks that showed up in the quarterly results that management attempted to downplay. With $2.5 billion in excess capital and with allowance for loan losses and net charge-offs way lower than its peers, it would be easy to overlook growing evidence that PBCT is not totally immune to the troubles plaguing other banks.

The most notable evidence that the recession is just now starting to show up in the otherwise stellar PBCT numbers is that non-performing assets jumped over 50% sequentially in the 1Q09, from $93.7 million at 12/31/08 to $142 million at 03/31/09. Most of the $48 million increase in non-performing assets was in commercial real estate ($24 million) and residential mortgages ($18 million).

Figure 2. PBCT Total Non-Performing Assets, 1Q08 through 1Q09, Millions of $. Source: PBCT SEC Filings.



Before getting to the details, its worth noting that management tried to head off any concerns over the numbers during the 1Q09 conference call by reminding investors that its metrics are far superior to its banking peers. With regard to the jump in non-performing assets, CFO **Paul Burner** made the following comment during his prepared remarks at the beginning of the call:

> As you can see on slide 10, our NPAs [non-performing assets] increased from 64 basis points in the fourth quarter to 97 basis points this quarter. While this appears in isolation to be a significant increase, you can see that it compares very favorably to the top 50 banks at 269 basis points and our peer group at 243 basis points as of year-end. In fact, our first-quarter NPAs are roughly 1/3 of those of the top 50 banks as of the fourth quarter…

Looking more closely at the numbers, half the increase in non-performing assets was in the commercial real estate portfolio. The bulk of the increase ($16 million) came from a single credit in its Shared National Credits (SNC) portfolio that got moved into non-performing. The loan is for a mixed-use development project "in the South" (management refuses to say exactly where, but it does say it is *not* Florida) consisting of office and retail space, apartments and condos. When asked if the Company had taken a loan loss reserve on the credit, CFO Burner replied:

> No, we did not. Actually we feel very good about the project. That is what I was trying to do by giving you examples there. I personally believe we will get out of that without a loss.

The SNC portfolio was initially established to expand geographic diversity in the loan portfolio, and has been in run-off mode since the beginning of 2008 and is expected to be unwound in two to three years. At 03/31/09, the SNC portfolio stood at $672 million, which is actually up slightly from 12/31/08 when it stood at $664 million. About 44% of the portfolio consists of commercial real estate loans.

Towards the end of his prepared remarks, Burner admitted that another loan from the SNC portfolio had moved to non-performing after the quarter ended, so it was not included in the $142 million non-performing asset number at 03/31/09. We thought his comment on the situation interesting [bolding is ours]:

> The sales, as we have said in the past, given the depth of economic weakness being experienced nationwide, we do not expect to remain insulated from credit losses or credit issues and losses. In fact, subsequent to quarter end, a second real estate related to shared national credits in the amount of $16.9 million has migrated to non-performing status. **This is part of our remaining $36 million in exposure in Florida.** The building is complete and partially occupied, but the **majority of presales with 20% down payment** have been either unable or unwilling to close.
>
> In fact, we have done a loan by loan analysis of the entire shared national credit portfolio and **do not feel any undue concerns**.

We're not exactly sure what Burner means when he says they "do not feel any undue concern", but we wouldn't be too optimistic about a Florida project where people are apparently walking away from 20% down payments. When thinking about these two recent additions to non-performing assets that totaled $32.9 million from the SNC portfolio, it's worth keeping in mind that total allowance for loan losses at 03/31/09 stood at $159 million, just 1.09% of total loans.

As for the increase in non-performing residential mortgages, the balance at 03/31/09 grew nearly 75% sequentially, from 77 basis points to 138 basis points of total residential mortgages. Management, of course, is quick to point out this is a much smaller ratio than the national average or among its peers. They are also quick to point out a number of other factors designed to assuage any concern in the jump, such as the fact that 75% of the non-performing residential mortgages have LTV ratios below 90%, suggesting relatively low loss content.

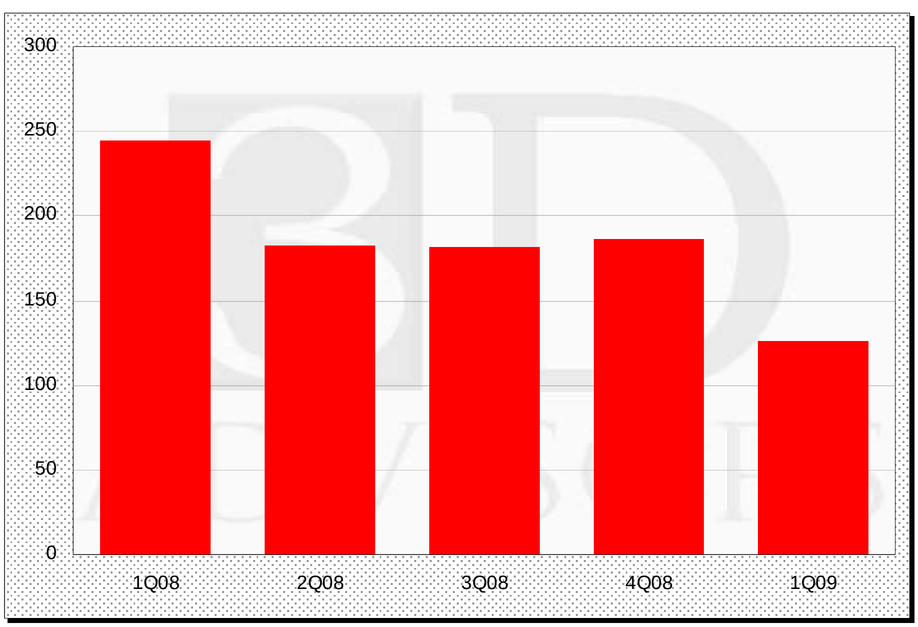
While it is certainly true that the metrics management cites for itself are significantly stronger than its peers, and net charge-offs remain very low, there is no doubt that non-performing commercial real estate loans and residential mortgages both jumped in 1Q09. Non-performing commercial real estate loans went up 80% (from $29.8 to $53.8 million), while non-performing residential mortgages surged 75% (from $24.2 to $42.3 million). There is no hiding these facts.

Accounting: Non-performing assets jump, but reserves and charge-offs stay low

One of the things that stood out in the 1Q09 results is that despite the big sequential jump in non-performing assets, the allowance for loan losses remained flat at $7.9 million, or just 1.09% of total loans. In effect, by not increasing the allowance in the face of a much higher level of non-performing loans, the Company is betting that it will not be forced to take *any* losses on the loans that moved to non-performing.

A statistic the Company itself disclosed in the 1Q09 SEC Form 10-Q is the ratio of the allowance for loan losses to non-performing assets. While the ratio remained stable through the last three quarters of 2008, the drop in 1Q09 is abrupt. In fact, the ratio is almost half of what it was in 1Q08.

Figure 3. PBCT Ratio of Allowance for Loan Losses to Total Non-Performing Loans, 1Q08 through 1Q09. Source: PBCT 1Q09 SEC Form 10-Q.



An interesting exchange took place between an analyst and CEO Sherringham during the 1Q09 conference call on this very statistic.

> **Analyst:** One of my questions was on the yields, and so that was just answered. A follow-up question that I have is on the reserve to loan ratio and how do you look at that? As we move forward, as we see increased -- I believe, the ratio that was presented in the PowerPoint presentation was the reserves to nonperforming assets or nonperforming loans. Do you look at it mostly on that basis, or do you also --?
>
> **Philip Sherringham, CEO:** No, no, actually I'm glad you brought up the issue. The more meaningful measure to us is the ratio of reserves to total loan portfolio, which went up a little bit to 109. We mostly reserve a little bit [inaudible] as you know.
>
> And there I would say that obviously we have a very robust methodology to determine loan adequacy. We keep fine-tuning it to improve the current environment, but basically we are extremely comfortable with our overall reserving position. The ratio that is, in fact, less meaningful is the ratio of reserves to nonperformers. Candidly, especially in our case, because the base is so low. So all it takes is one or two credits either to move up or down, to be cured or to go bad, if you will, to move the ratio very meaningfully. So that ratio to me for a bank our size given our exposure is much less meaningful. It will swing pretty widely one way or another. The one I'd focus on would be the ratio of reserves to total loans.

To our point of view, his answer makes no sense and seems a departure from PBCT's conservative reputation. Non-performing loans are undoubtedly going to continue to rise as the economy stays weak. If the non-performing loans are going up and getting older it would make more sense to carve out of the total allowance an amount sufficient to cover at least some of those more likely losses. Then they could see how much allowance is available to cover the rest of the portfolio. If the mix of a loan portfolio changes in terms of performing versus non-performing assets, looking at the total allowance and keeping it at the same level based on the total portfolio amount makes no sense. The probability laws can't be ignored.

<u>Insider Trading: Commercial group chief and spouse sell almost entire stake</u>

The key seller in 2009, and more specifically this quarter, was the above-mentioned head of the Commercial Banking division, Brian Dreyer, a bank employee of almost 30 years. Dreyer has an interesting trading history since the thrift conversion, having first paid $20 to buy shares in the April 2007 initial offering only to sell the acquired shares at a loss ($17.90) five months later, a pattern he shared with several other executives which we initially covered in an IRB on 11/18/08. Since then he has been a frequent seller, having now traded in five of the last six open trading windows. In addition to clearing out the majority of his vested options and more than half of his common in 4Q08, including shares that had vested in October, he also moved all 3,900 Excess Benefit Plan investment units, which were scheduled to convert to PBCT shares after retirement, into a fixed rate investment. In total he distributed 123,000 shares between October and December at prices up to $18.

Dreyer resurfaced again in the current quarter with new actionable equity at his disposal after additional shares from stock awards became unrestricted earlier this year. With two-thirds of the quarter in the books, Dreyer sold 25,000 shares on 05/27/09, including 1,000 shares owned by his wife (more on her later). The trades were executed at a 15% discount to his last sale in December. He would then trade again on 05/29/09 and 06/01/09, selling another 14,122 shares of his direct holdings while his wife cleared out all 14,213 of her remaining shares all in the $15 range. The only shares Dreyer left untouched were the 2,300 shares held in his 401(k) and purchased through the ESOP. He does still retain a handful of vested options, but the majority is either out of the money or very close to slipping under water. The sales by the Dreyer household since the fourth quarter erased 90% of their combined actionable holdings.

We mention Dreyer's wife because the 144 filed for her sales reveals her as **Ellen Davis**, the former Senior Vice President of the Commercial Banking division and also head of the Shared National Credits portfolio highlighted above. This was very interesting new information to us on a number of fronts. For one, it has never been disclosed in the Related Party Transactions section of the Company's Proxy Statements or in any other corporate filing that Dreyer had a relative employed by People's, which is a filing requirement for any such relationship of a named executive officer under Item 404 of Regulation S-K. The obfuscation is even more significant considering Davis likely reported directly to her husband until her resignation in early 2008. And while she is no longer employed by People's, she is obviously still well-informed of the Company's operations, which makes her recent disposition that much more interesting.

There have also been a number of directors who took profits in the current quarter. The board is comprised of 10 independent members, five of whom collectively sold 35,000 shares between 04/28/09 and 06/11/09 at an average price of $16. One interesting connection between the sellers is that four of them sit on the Operational Risk Committee, which is charged with overseeing the Bank's risk function and "the processes and systems developed by the Bank to assess, monitor and mitigate operational risk". In the current environment these are not the individuals one would want to see taking profits in concert, particularly as they have accepted the lowest prices associated with any of their sales to date. Director **James Thomas**, who also chairs both the Compensation Committee and Nominating Committee, surfaced with his first sale since paying $20 for shares in the initial offering. He took a 22% haircut to sell 6,450 shares on 06/11/09 at $15.66. Chairman of the Audit Committee **George Carter** sold 5,873 shares on 05/12/09 at $16.58 and has now averaged down with each of his last three trades after initially buying stock in April 2007 at $20. And finally, **Jerry Franklin**, who holds a seat on nearly every board committee, executed his largest sale yet on 06/11/09, distributing 8,000 shares at $15 after selling at $17 last August. Each of these directors has served the Company for over ten years.

To recap, we have the first significant cracks appearing in the PBCT story in 1Q09 in the form of a dramatic increase in non-performing assets, concentrated in its commercial real estate and residential mortgage portfolios. In response, management attempts to draw attention away from the obvious decline in asset quality by reminding investors that its performance metrics are still far superior to its peers, while choosing not to increase its allowance to reflect the big rise in non-performing loans. Meanwhile, the long-tenured head of commercial banking drops almost his entire actionable position at significantly lower prices and on top of that we learn his wife, a former PBCT employee who ran the Shared National Credits portfolio and whose relationship with her husband was never disclosed by the Company, at the same time sold off her remaining holdings as well. Suffice it to say, we will continue to monitor developments closely, and we would advise interested clients to do the same.