BACK TO SCHOOL

by Steve Brown

With summer just around the corner, we were dismayed to hear that despite years more in education, diplomas, certifications and other credentials, hundreds of professional money managers lost out to an 8th grade class from Seattle in a national stock picking contest. The kids not only beat the S&P 500 Index (which increased 2.38%) and hundreds of professional investors, but they also created a hypothetical portfolio of stocks that soared nearly 26% during the contest period. Not bad for a bunch of wet-behind-the-ear kids that probably often head off to school with their shirts un-tucked and shoes untied. This got us wondering about the banking industry, as we pondered where it might be heading over the next few years. As we discussed our recommendations for bankers to consider in coming years, we wondered if we were being too analytical. So, we too solicited the help of a class of 8th graders, rather than rely merely on detailed studies, surveys and industry research. As we have uncovered, bankers hoping for a period of calm and fat profits over the next few years will have to adjust their expectations and brace for an even faster pace of change in the industry. As if remote capture and loan conduits were not enough to deal with, the industry continues to radically change the way it does business. While much has yet to play out, independent bankers should be prepared to deal with significant changes, including: 1) Increasing burden of regulatory compliance Â– bankers will have to adopt a risk management approach. Greater regulatory scrutiny, new regulations and more board involvement are all key considerations bankers will have to incorporate into their daily business dealings to remain at the top of the performance spectrum. A robust risk management platform is a good starting point. 2) Falling net interest margin Â– bankers are facing an increasing pool of competitors, heightening pressure to expand into new geographic areas and product lines, while fundamentally dissecting cost structures. Independent bankers are slowly embracing offshoring to improve efficiency and reduce costs, while leveraging technology to streamline processes. 3) Embedded technology Â– bankers have realized one of the best ways to fight strong competition is to leverage technology wherever possible. By working closely with employees and customers, bankers are reinventing processes and finding technological solutions to leverage scarce resources and improve effectiveness. Remote capture, mobile banking, integrated loan automation systems and enhanced credit scoring of smaller loans are but a few of such technologically-enhanced product and service offerings bankers should consider. To improve performance, bankers will need to monitor and continually improve on technological enhancements as they evaluate new strategic initiatives. Bankers should review product and service delivery from the customer all the way through the organization including back-office processing to maximize opportunities and enhance delivery methods. Beyond the traditional efficiency ratio, bankers will have to find ways to cut costs, while improving the customer experience and increasing growth. It is time to go back to school and learn something from the 8th graders Â– bankers should remain flexible, be open to new ideas, eliminate preconceived notions and work together as a team to ensure success. Now, get on the bus because we have work to do and the bell is already ringing in the distance.

BANK NEWS

M&A

Central Bancompany ($7.8B, MO) will acquire the 5-branch Metcalf Bancshares ($280mm, KS) for $75mm in cash, or about 3.1x book.

35% Tax Bonus

The loosening of S-Corp rules were tacked onto the latest spending bill that sailed through the Senate and is expected to be approved by the President. The new provisions would allow for more classes of shares that S-Corps can issue and change the treatment of some expense/capital gain items. The changes should increase the number of banks that choose the designation slightly.

CU Expansion

The NCUA proposed allowing community chartered credit unions to expand their geographical definition from its current MSA standard to a much larger "core-based statistical area."

Regulatory

MN has enacted a law that will make merchants who do not protect credit card data liable for financial reimbursement for losses stemming from any data security breach. MN is the first state in the nation to enact such a law.

Basel II

The FDIC said again that it does not expect Basel II to disadvantage U.S. banks. Citing an academic study suggesting profitability and capital are positively correlated, the FDIC said that since U.S. banks are better capitalized than their foreign counterparts, they are also in a position to outshine such competitors.

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Royal Bank of Scotland, Santander Central Hispano and Fortis jointly offered approximately $95.6B for ABN Amro in both cash and stock. This trumps Barclays' all-stock offer by 10% and calls into question the sale of ABN's LaSalle unit to Bank of America.