

## Getting Back to Basics

At the recent *American Banker* Best Practices in Retail Financial Services Symposium, one consistent theme was that banks need to get "back to basics". We agree. At CPG, we believe this means that banks must:

- 1. Shift incentives toward service.** In this environment, front line staff in the branches should be encouraged to spend time talking to customers without the conflicts that arise when they have stretch sales goals to meet.
- 2. Pull consumer credit back into the relationship discussion.** Customers with good credit histories who can repay their loans will still need to buy cars and homes, pay for college, and finance other purchases.

Mortgages, credit cards, student loans, and the like are now ripe for integration into the relationship aspect of regional and community bank value propositions.

- 3. Get proactive about customer advocacy.** From the CEO to the teller, the message now needs to be: we can help and we will work with you to get you back on your feet. Building relationships now means taking the time to sit down with customers, review their current situation in detail, and help them set goals and identify strategies to rebuild.
- 4. Put employees first, and customers second.** Take a lesson from Southwest Airlines, one of America's most admired companies.

If you want to excel at customer service, make employee satisfaction your number one priority.

- 5. Put a big push on PR and communication and do it NOW.** Get the word out that your bank is THE place to go for information, assistance, and solutions. The investment banks are gone; many big banks are pre-occupied with merger integration issues; U.S. economic news remains grim; and consumers are focused on the security of their financial providers, not price. There is an unprecedented opportunity for traditional banks to build share by re-energizing the relationship banking model - but you need to act now!

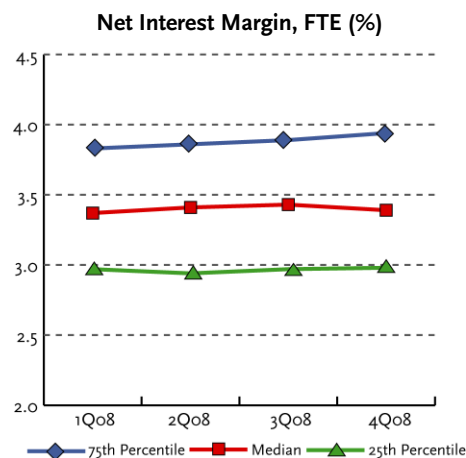
## Bank Performance Barometer Snapshot: Banks with assets \$5B-\$20B

Both the yield on earning assets and the cost of funds declined in 2008 at most mid-size banks and thrifts – those with total assets of between \$5 billion and \$20 billion – as the Federal Reserve lowered interest rates. This placed a slight downward pressure on margins. Institutions that posted a net interest margin at or above the 75th percentile (3.94%) were those who were able to significantly decrease their cost of funds by year-end.

**4Q08 Top Performer:** SVB Financial (CA) benefited from increased deposit growth in 4Q08. This allowed it to replace borrowings and brokered deposits, thereby lowering the bank's overall cost of funds. SVB also benefited from a focus on high-yield commercial lending. The bank targets niche industry sectors (technology, biotech, premium wine, etc.).

**Most Notable Improvement, 3Q08 TO 4Q08:** American Savings Bank, F.S.B. (HI) also lowered its cost of non-deposit borrowings and brought its NIM from 3.71% to 3.83%.

**CPG's Bank Performance Barometer™** tracks the performance of banks and thrifts on a quarterly basis. The report identifies top performers across 16 different metrics (including NIM, shown at right) and provides insight on how these institutions achieved success. Each quarter, the report also provides an in-depth look at a pressing industry issue and the strategies that we believe banks will need to use to address that issue – in 4Q08, for example, we focus on deposit gathering. To find out more about the **Barometer** or to order the full 4Q08 report, please contact Vanessa Mambrino at 202-337-1507 or [vmambrino@capitalperform.com](mailto:vmambrino@capitalperform.com).



### 2008's Top Performers

2008 Rank	2007 Rank	2006 Rank	Institution	Net Interest Margin (FTE) YTD (%)		
				4Q2008	3Q2008	2007
1	1	1	SVB Financial Group (CA)	5.66	5.74	7.14
2	5	6	Glacier Bancorp, Inc. (MT)	4.93	4.90	4.77
3	2	2	Pacific Capital Bancorp (CA)	4.91	5.54	5.30
4	7	8	Cullen/Frost Bankers, Inc. (TX)	4.71	4.69	4.71
5	4	5	Sterling Bancshares, Inc. (TX)	4.56	4.59	4.78
75th Percentile				3.94	3.89	3.96
Median				3.39	3.43	3.96
25th Percentile				2.98	2.97	3.10

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 The Wire is also available online. Capital Performance Group, LLC (CPG) is a management consulting firm headquartered in Washington, DC.  
 CPG offers consulting, analytic, and research services to clients in the financial services industry.

## Community & Regional Banks Have Unprecedented Opportunity

While the financial services industry, as a whole, has suffered over the last few months, well-positioned community and regional banks have been able to benefit from the plight of their larger competitors and attract disaffected customers. In fact, the events of the last year have significantly altered a number of performance trends (as seen in the table below).

The narrowing of the large bank-small bank performance gaps creates an unprecedented opportunity for community and smaller banks. Regional banks would be wise to begin figuring out how to sustain current fortunes and create marketplace separation going forward. Specific opportunities for smaller banks include:

**Segment-based strategies.** Banks that can demonstrate a keen understanding of customer needs and put forth a unique set of capabilities that align with those needs can command higher pricing and become the provider of choice for economically attractive segments such as Gen Y, medical professionals, not-for-profits, and small business owners, to name a few. Focus on these segments will help to spur the innovation of new products and ancillary

services that will be critical to creating competitive advantage.

### Streamlined sales and service processes.

Broader sales goals, the introduction of new technologies, and increased compliance regulations have all complicated the branch experience at many banks. Few banks have been able to adapt sales and service platforms to address these environmental changes, and instead, rely on the skills of their associate staff to create an image of integration to customers. Banks that can create a superior customer experience will achieve greater loyalty, and, ultimately, profitability. However, doing so going forward requires enhancement of end-to-end sales and service processes.

### Invoking more institutional discipline.

Smaller banks often put themselves at a disadvantage by being less measurement-focused and standardized. Management practices that suffice banks with one or two branch offices are typically sustained as the bank grows, and consequently, performance tends to become more disparate across the franchise. Small banks can maintain inherent advantages such

as localized decision making while ensuring more consistent customer experience through documentation of operational protocols and process monitoring. In addition, banks can achieve greater productivity through implementation of performance scorecards and more structured budgeting and review processes.

**Commercial deposit generation.** Banks large and small continue to underwhelm commercial deposit opportunities. Many banks are offering strong incentives to new loan and loan renewal customers to move their deposit relationships to their credit provider, yet the majority of commercial RMs continue to be credit focused. Treasury product specialists have become the de facto commercial deposit specialists for a lot of banks, yet these individuals tend to be very product focused and charged with helping RMs to cross-sell into credit relationships. Banks need to take a more customer-focused and proactive approach and develop an acquisition-focused sales team that can identify deposit opportunities and speak to customer cash management and information needs.

### Median Performance of Large (> \$20B assets) vs. Small (<= \$20B assets) Financial Institutions

Metric	Before: 2005-07 Performance Leader	Now: 2008 Performance Leader	Reality of the Situation
Return on Average Equity	Large Banks	Small Banks	Asset write-downs driving sharp bank declines while smaller banks experiencing slower, steady decline
Noninterest Income/Operating Revenue	Large Banks	Large Banks, but gap narrowing	Large bank fee contribution has decreased; smaller banks have made no real improvement
Net Interest Margin	Small Banks	Small Banks	NIMs are declining steadily across all asset sizes; concern is greater for smaller, more NIM-dependent institutions
Core Deposit Growth	Large Banks	Large Banks, but Small Banks improving steadily	Large banks 2008 median growth rate was over 2x that of smaller banks, but safety and soundness concerns playing to small banks advantage
Noninterest Expense/Average Assets	Large Banks	Small Banks	Small banks have made virtually no improvement since 2005 but now lead because of large bank expense increases
Loan Loss Reserve/Non-performing Assets & 90+ Day Delinquent	Large Banks	Small Banks, but gap is very small	Ratio plummeted for both groups; 2008 almost a dead heat

Source: Commentary based upon CPG analysis of SNL Financial data as of March 2009.

## Regulatory Corner: CPG's Take on Events from inside the Beltway

Up until the announcement of the Public-Private Partnership Investment Program (PPPPI) on March 23rd, many in the press and on Capitol Hill were unconvinced of the overall effectiveness of the Treasury Department's efforts to address the financial crisis. The kerfuffle over the bonuses paid out at AIG prompted Representative Connie Mack (R-FL) to make the following statement:

"This week's news on the AIG bonus scandal is but the latest fiasco under his watch and he has lost the confidence of the American people. Quite simply, the Timothy Geithner experience has been a disaster. The Treasury Department is in disarray. Taxpayer dollars are being wasted. America's economy hangs in the balance. America needs and deserves a Treasury Secretary who can truly lead us forward. Timothy Geithner should either resign or be fired for the good of the country, and President Obama should nominate a new Treasury Secretary with the experience and leadership skills America deserves."

President Obama has stood by Mr. Geithner and the Treasury Secretary's proposal to deal with toxic (or "legacy") assets has met with a generally favorable reaction from investors. We at CPG disagree with Rep. Mack; however, we believe that the events of March 2008 are a sign that the Treasury needs to improve its communications efforts and provide greater clarity to the public and the press in order to regain the confidence that will be necessary for its overall schemes to work.

### Announcements

In the 17th annual *ABA Banking Journal* Top Performers ranking, CPG's Vanessa Mambriano reviews the performance of the nation's best banks. Look for the top 25 big banks in the May issue and the best community banks in the June issue.

**CPG's Retail Competitive Tracker** will enable your team to delivery consistent, informed responses to the one question that matters most: **"Why should I bank with you?"**. For more information, visit our website - [www.capitalperform.com/tracker.htm](http://www.capitalperform.com/tracker.htm).