

Dr. Ed Seifried Shares His 2010 Industry Outlook with CEOs

We asked Dr. Ed what bank CEOs should be concerned about in the coming year and without a moment's hesitation he started articulating a list of items. He suggests we take a short term and short-to-longer term perspective as we anticipate the effect of the sluggishly recovering economy on community banking. He points out that we must watch economies around the world as well as national and regional ones. Most significant, he believes, is the economic condition of your local community, one of the most influential factors on your strategy going forward.

Short-Term Focus

He sees six areas that CEOs should focus on in the short term. Dr. Ed suggests that by short term he means 1-3 years during which you attend to your most immediate concerns. And, again, he says, "don't underestimate the importance of your bank's local economy in contemplating your bank's 2010 strategy. The unemployment rate is your primary indicator for that."

Here is Dr. Ed's preliminary list every CEO should be actively monitoring in the short term:

- 1. Recalibrate your strategy downward.** Dr. Ed cautions that your loan and deposit growth expectations must be realistic. If your community is experiencing a jobless recovery, for example, the Board and Senior Management need to recognize this will impact any growth expectations for the future.
- 2. Protect your loan portfolio.** He recommends that you maintain a "toned down" forecast for loan profitability for the coming year. This is especially true if you are located in a state that is seeing double digit unemployment because

major industries have been affected (the obvious one is Michigan). And be careful with your underwriting practices during this time period as you don't want less than ideal loan decisions to come back and haunt you.

- 3. Pay attention to staff morale.** As Dr. Ed says, "nonperforming loans can become a Human Resources problem because if you blame the loan officer for the loan's performance in place of recognizing the role of the recession, you'll have marginalized a group of employees by doing so." In the end, you want to delicately address the nonperforming loans with your loan officers given the current environment. Management should make a concerted effort to understand the loan officer's perspective and to appreciate how much of the spotlight is already on them.
- 4. Monitor other factors that distress customers.** Beyond unemployment, there are other local and even global events that can contribute to your customers' financial distress. Think about how agriculture prices, energy costs, and cut backs in government spending, for instance, could cause further stress for your customer base. Whenever there is a major or abrupt change in any one of these areas, your customers' response and banking-related behavior will no doubt be a rough measure of the severity of the problem.
- 5. Review your institution's investment portfolio.** Dr. Ed says "as the loan portfolio shrinks as a percent of assets, and more is in investments, managing risk becomes more of a necessity." "Consider a third-party audit for your review to ensure an independent assessment of the institution's investment strategies and risk exposures."
- 6. Reemphasize asset liability management.** We've all become rather complacent, Dr. Ed,

suggests, but with a recovering economy comes the specter of higher rates, and it is time to go back to the conventional asset and liability management model. He is concerned we have turned our backs on this exercise and need to revisit it now.

Short-to-Long Term Focus

Dr. Ed doesn't see a distinct cut off from when immediate concerns dissipate and longer ones show their face; it is more of a continuum, where they blend together and reformulate as time goes on. Having said that, here are some longer term issues CEOs should think about:

- 1. Health of the economy.** At best we don't want to find ourselves too much like Europe in that they've accepted "subdued economic growth" for the long haul, says Dr. Ed. We have to hope the slow recovery picks up, rates rise, and this is all in our rear view mirror.
- 2. Legal and regulatory changes.** Health care reform, financial regulatory reform, restructuring the banking agencies, and any other ambitious changes will leave an indelible imprint on the banking community.
- 3. Non-interest income challenge.** Between the new overdraft rules, more consumer protection legislation, and other like challenges to fee

income, banks will need to be more innovative in generating non-interest income for the time being.

- 4. Reputational risk for banks.** Even President Obama has attempted to convince the public that community banks are not responsible for the securitized financial instruments that shattered Wall Street nor did they allow the Federal government to bail them out, nor are they the ones receiving extraordinary compensation packages. Just the same, CEOs want to guard against this type of reputational risk by communicating to your customers, the press, and the community that your bank is separate and distinct from the investment banks and mortgage companies that caused our economic crisis.
- 5. Interest on Excess Reserves.** Dr. Ed says CEOs "should follow what the Fed is doing closely—especially the IOER (Interest on Excess Reserves) program." He adds, "deciding whether or not to participate in the proposed "interest on reserves" program, and if so, to what extent, may be similar to the confusion surrounding the question of whether community bank should participate in the TARP program!" He urges CEO's to investigate and anticipate the income and balance sheet effects of the program. ■

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Dr. Seifried served as Professor of Economics and Business at Lafayette College in Easton, Pennsylvania for over 25 years and is currently Executive Director of the Sheshunoff Affiliation Programs. In addition, Dr. Seifried is the Chief Economist for m.rae resources, inc., a strategic and financial services firm for community banks. He received his doctorate in economics and business from West Virginia University.

Dr. Seifried serves as the dean of the Virginia and West Virginia Banking Schools and is a faculty member of numerous banking schools including: Stonier Graduate School of Banking, and the Graduate School of Retail Bank Management.

He frequently appears as a guest speaker at regional and national conferences and has delivered over 2000 presentations to various groups both in the United States and abroad. Dr. Seifried is a consultant to the banking industry, and is well known as a speaker at bank customer events and as a strategic planner. Dr. Seifried is the author of the book "The Art of Strategic Planning for Community Banks." In addition to his academic and consulting experience, Dr. Seifried has also served as a director of a community bank.

Dr. Seifried has traveled extensively in the former Soviet Bloc countries where he served as an advisor and consultant to the newly privatized commercial banks.

