

## Where Will Revenue Come From in 2009?

By, Thomas W. Grottke, President  
Northeastern Banking Services Group, LLC



In recent interactions with our clients, we have heard an almost universal concern from bank executives regarding the serious pressures on their budgeted, forecasted or pro-forma 2009 operating income. Most executives expect that operating expenses will continue to rise, while revenues are expected to remain flat or decline in nearly every business and product line. You don't have to be an accountant to figure out that such an equation equals a decline in operating income. Aggravating the profitability situation is the growing risk of deteriorating asset quality driving up loan loss provisions, further investment securities write-downs and added loan and real estate work-out costs.

This commentary is not on "bad bank" issues - you can read about those topics anywhere - but rather about where and how to maintain profitability of your core banking business when your opponent, the external environment, just hit a grand slam with interest rate, credit risk, economic and regulatory environments hitting your bank's businesses at breakneck speed.

### ***Core Bank Operations***

From an operating perspective, yields on quality bankable investment securities are negligible; commercial real estate mortgage activity is expected to be modest, if much at all; C&I loan yields, even with floors, are at historical lows; consumer lending is non-existent; residential mortgage yields are back to near historical lows, and fees on deposits continue to be squeezed by relentless competition for core deposits in most markets. Some institutions have the potential luxury of other non-traditional product lines such as Mortgage Banking, Trust, Insurance Agency, Check/Lock-box Processing, Brokerage, Leasing, Agribusiness and other niches. But a closer look at many of these product lines show potential concerns with revenue growth and/or growing expenses.

You may not be in this situation and, if you are not, consider yourself extremely lucky. Maybe you should patent your operating model and sell it to make even more money for your institution! But our expectation at NEBSG is that your financial institution is also expecting and beginning to endure the same revenue trends.

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### ***So what can you do to minimize these negative financial trends?***

We may finally be at the point where other sources of revenues are becoming an absolute necessity in banking. However, turning on new lines of fee-based businesses takes time, immediately increases expenses and adds systems, operational, reporting and compliance requirements to an overly loaded back-office.

Even though my comments today are on the revenue side, I would be remiss in not emphasizing the importance of dealing with the cost side of the equation. We recommend the obvious from an expense perspective – non-interest expense control/reductions; close attention to asset quality (manage the investment and loan portfolios extremely close); competitive rebidding of all major contracts; out-sourcing functions where cost savings and economies of scale can be immediately and continuously realized; holding-off on added physical plant additions/openings (if possible); and avoiding paying up for deposits.

But for those banks with strong capital and minimal asset quality issues, we recommend an aggressive approach to gain market share and to add competitive products and services. Now is the time for healthier banks to get ahead of those who may be struggling (besides some community banks, many regional and large banks are seriously struggling and cutting back on sales and product development to weather the storm).

For winning new **consumer customers** or expanding existing consumer account relationships, we recommend continuous market awareness/brand promotion capitalizing on financial strength, staying power and local presence, coupled with a two pronged sales focus:

- (1) Active residential lending program with government programs (such as FHA and state programs), selling the mortgage balance in the secondary market, retaining loan servicing for selected customers with desirable geographic proximity to your franchise or a willingness to have a full service relationship with your bank by tying their mortgage to mandatory checking accounts with direct deposit, automatic monthly loan payments and E-Statements; and
- (2) Rolling out an expanded and highly competitive Internet Banking product and service set (e.g., on-line account opening, on-line loan applications, Mobile Banking, Account Aggregation, person-to-person bill pay, etc.).

For **small business customers**, we recommend an increased business development program with branch personnel, Business Development Officers, lenders and cash management product specialists offering full service banking relationships with risk based line of credit pricing (based, of course, on credit scoring and an appropriate automated loan underwriting program for lines of credit) coupled and tied to minimum deposit relationships and added e-services. Originating C&I loans and lines with interest rate floors and modest fees requiring the transfer of commercial DDA and signed-up use of other business

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services (e.g., Internet Banking, payroll processing, automated returned check collection, and other modern features) to gather core deposits.

You may say to yourself that these two strategies are not new or unique. However, what we are seeing is a pulling back, uncertainty of direction, increased fear of these kinds of traditional credit products with generally reasonable risks, and a continued stifling of growth in low-cost core deposits. We are not seeing many healthy community and regional banks capitalize on today's market opportunities.

Actively moving on these two business development strategies does not require new or different resources for the typical community or regional bank. Residential lending, consumer DDA, small business C&I and DDA products are in your holster and within your capabilities. But focusing your management team in a coordinated manner to quickly refocus and double your efforts may require some resources and utilizing your sales culture by driving customer activity into your branches to position your personnel to cross-sell your products is always beneficial.

As the shake-out in the financial services industry continues, survival is job #1. But once you are certain of your survival, it is time to move ahead while many of your competitors are down. This can be the competitive advantage you have been waiting on for many years.

*Mr. Grottke provides strategic services to community and regional banks. His firm, NEBSG, has the experienced professionals you need to help get your projects launched and executed as well as the depth of expertise to provide strategies, tactics, technical systems guidance and regulatory and operational skills to help you quickly get your action plans up, running and completed in a cost effective manner. Visit our web-site at [www.nebsg.com](http://www.nebsg.com) or call us at 860-436-6149.*