



TKG Perspective

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Teaching/Speaking Engagements

Pennsylvania Bankers Association
PBA Advanced School of Banking
Penn State
State College, PA **July 11-16**
How do Banks Make Money?

Pennsylvania Bankers Association
PBA School of Commercial Lending
Penn State
State College, PA **July 25-30**
Problem Loans

Maryland Bankers Association
The Maryland Banking School
University of Maryland
College Park, MD **August 1-6**
Bank Financial Principles

Financial Mangers Society
Controllers Clinic
Hotel Sax Chicago
Chicago, IL **August 16-17**
Improving the Budgeting Process

Pennsylvania Association of Community Bankers
133rd Annual Convention
The Breakers
Palm Beach, FL **August 28-31**
Making More Products and Lines of Business Profitable

PNC Bank
Correspondent Banking Conference
Skytop Lodge
Skytop, PA **September 14-16**
The Current State of Community Bank Profitability and Performance

Maine Bankers Association
Annual Convention
Mount Washington Resort Hotel
Bretton, NH **September 17**
Profitability & Performance Measurement

PICPA
Harrisburg, PA **September 27**
Profitability and Future Trends in Banking

2010 Conferences and Conventions

New Jersey Bankers Association
Annual Golf Outing
Forsgate Country Club
Monroe Township, NJ **August 9**

Pennsylvania Association of Community Bankers
Annual Convention
The Breakers
Palm Beach, FL **August 27-31**

New Jersey Bankers Association
Senior Management Conference
Seaview Resort & Spa
Galloway, NJ **September 22-24**

New York Bankers Association
Annual Convention
New York, NY **November 8-10**

Keeping things in Perspective

By Robert E. Kafafian

The last few years have certainly been a difficult time for the financial industry, as well as the United States and world economies. The sub-prime fiasco has been compared to the great depression and the final chapter of this story is yet to be written. History will eventually provide us with a rear-view mirror someday, and perhaps we can then put it all into better perspective.

We as humans have a habit of thinking when bad things happen that what we are experiencing are the worst of all times. However, a look at other past events may prove otherwise.

DORIS KEARNS GOODWIN

I'm reminded of hearing the noted author and historian Doris Kearns Goodwin speak at a conference a few years after 9/11. She was asked if the event of 9/11 was the worst time in history. She slightly smiled as she thought about her answer and said, "No, 9/11 isn't necessarily the worst event in history. It only seems that way to us as we live through it in real time, and don't yet have the benefit of knowing the ultimate outcome which history will eventually answer."

She went on to say, "Imagine the uncertainty George Washington and his army felt fighting the British with the ultimate independence of what we now know as the United States of America at stake. Imagine how Abraham Lincoln felt at the beginning of the civil war, worried that the country as he knew it might not survive. Imagine how unemployed and bankrupt citizens felt after the great depression of 1929 wondering whether life as they knew it would ever be the same. And imagine how the world felt in the late 1930's, not knowing that Adolph Hitler would ultimately fail."

You see, our country and the world has been through so much and, let's not kid ourselves, more is going to happen. Yet, the United States is still the best country in the world. Our people and economy are very resilient and we will continue to survive and ultimately thrive. But, without a doubt, there will always be a few curves in the road.

JAMIE DIMON AND PREPARATION

In the fall of 2009, I had the opportunity to attend and moderate a panel at the New York Bankers Association's Annual Convention. One of the keynote speakers was Jamie Dimon, the CEO of JP Morgan Chase. He was captivating, forward thinking, and an amazing speaker. He is also an incredible executive, manager, and leader.

He was asked about the depth and length of the current economic crisis, and about his opinion and perspective for the future of our economy, and particularly for the banking industry. He said that in early 2009, his daughter, who was a college student at the time, asked him "How are we ever going to survive this crisis and aren't you worried about the economic situation and its impact?" He responded to his daughter by saying he was already focusing on mitigating the next crisis. How interesting is that?

Mr. Dimon, who happens to be the same age as me, went on to say that in his lifetime he had witnessed the following events:

- ✚ The oil embargo and gas lines of the 70's
- ✚ Interest rates hitting 21% in the early 80's
- ✚ The savings & loan crisis in the late 80's
- ✚ The commercial real estate crisis in the early 90's
- ✚ The dot.com crash around the year 2000
- ✚ The 9/11 terrorist attack
- ✚ The current sub-prime/real estate mess

He went on to say, “Do we really believe that nothing else is coming down the pike or going to happen?” He wouldn’t specifically predict what might be next, other than to speculate that it could have something to do with international commerce, unfortunately terrorism, and/or perhaps be IT related, (i.e. data security and other potential security breaches and frauds). But he was certain that he and JP Morgan Chase needed to plan and be prepared for whatever might occur.

Mr. Dimon also discussed how he manages and delegates in a trillion dollar company. He never takes his finger off the pulse of what is occurring in each line of business, but he also doesn’t micromanage, making sure he finds the best, most competent people he can trust. He meets with his senior team minimally by telephone on a weekly basis and has an all day face to face meeting on a monthly basis...almost like a mini strategic planning session. Ultimately, what I learned from his comments was that the secret to good management is being ready to manage through both good and bad times, and most of all being prepared and informed. He concluded that each of these events should become a learning experience for the next occurrence for the successful manager.

RISK MANAGEMENT

The comments of both Doris Kearns Goodwin and Jamie Dimon, along with the current state of affairs are why enterprise risk management has become such a critical and strategic focus in the banking industry. We need to recognize that risk management is much more than credit risk, although credit risk may be one of the highest priority risk factors. Additionally, managing risk is also about managing capital. The OCC and financial industry regulators have nine categories of risk that are part of every examination today. The following is a breakdown of these categories:

Credit Risk	Credit risk is traditionally the risk that loan borrowers will default on their obligation, but today it must also include the risks we take and the credit quality in the Investment Portfolio.
Interest Rate Risk	Born out of the savings and loan crisis of the 1980’s, interest rate risk focused financial institutions on asset and liability maturity mismatches, i.e. asset or liability sensitivity, fluctuating interest rates, and formalized the birth of the Asset/Liability Management process and the need for securitization.
Liquidity Risk	Liquidity Risk is the ability of a bank to meet its current and projected obligations.
Price Risk	This risk relates to Fair Value and Mark to Market Accounting and also directly relates to liquidity risk. For example, if a security is held to maturity, it mitigates price risk but can create liquidity risk. The converse is if a security is available for sale it will help liquidity but creates price risk.
Strategic Risk	This relates to overall strategic direction and board and management decision making with the emphasis on making informed decisions, not necessarily always making right decisions, which is impossible to do.
Reputation Risk	The industry has become tarnished by the failures of Countrywide, Washington Mutual, Lehman Brothers, etc. A negative or poor reputation can create significant challenges to successfully growing a profitable franchise.
Operational/ Transactional Risk	This risk is at the top of the list as it relates to international capital standards and the Basil Accord. The risk of data security, identity theft, fraud, international transfers, merger integration, and system conversions become increasingly critical the more dependent we become on technology in a world-wide economy.
Compliance Risk	As the regulatory burden in the financial industry continues to increase it seems almost daily the responsibility to be in compliance costs more time and money. Recently, given the climate in Washington, DC, the term Political Risk is also being born out of compliance risk.
Foreign Exchange Risk	This risk relates to the value and exchange of currencies world-wide.

FINAL THOUGHTS

I would also highlight that while bottom-line performance and profit are still the ultimate goal for all banks, safety and soundness and preservation of capital will continue to be the watch words for the next 12 to 24 months.

Consider the following trends as you plan for the long term:

- ♦ There is likely to be a surge in banking industry mergers and acquisitions.
- ♦ The rate of bank failures and government takeovers will remain far above the historical norm which is part of the reason for the surge in mergers and acquisitions.
- ♦ There will continue to be a growing acceptance of technology and online banking relationships and resulting branch network attrition.
- ♦ Regulators will continue to demand additional capital and reserves.
- ♦ The cost of regulation and compliance will continue to rise.



TKG, as part of our strategic planning engagements, periodically evaluates our industry, its trends, successes, and challenges. We are pleased to share our thoughts with you, our valued clients, in the form of this periodic newsletter. If you would like to discuss strategy further, or learn more about our performance measurement, strategic planning, profit/process improvement, or financial advisory services, please call us at (973) 299-0300 or visit us at www.kafafiangroup.com.