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BANK THINK

How Some Small Banks Thrive in a Tough Environment

By George W. Millward

Clearly the work required to operate a profitable institution in a safe and sound manner is becoming much more difficult. Some banks have not only just survived but thrived in the more stringent environment. Others competing in the same markets have purposefully laid the basis for their future growth. Yet a few banks have not done either. External forces are important factors to strategic success, but they do not explain why some banks succeed and others do not.

Management reviews conducted by my firm, The Kafafian Group, Inc., have provided some insights into what differentiates a thriving bank from a struggling one. Here are five key takeaways from our assessments:

- **Plan your work, work your plan.**

Many banks we reviewed have had a strategy of "just existing as a community bank."

Few bankers (management or board level) knew why they were in business or the type of business they wished to run. Setting and communicating a direction relevant to the market is essential for survival. An annual review of strategy enables a confirmation of the bank's direction, scope and pace of implementation. Just as important, it requires the courage to change the strategy when conditions demand it.

- **Understanding the culture is critical to success.**

Cultures drive where responsibility and accountability for decisions and actions rest. Examples of cultures found in these banks include the dominant chief executive officer, a de novo environment where responsibility is not clearly delegated or a lender-centric bank where credit decisions are the sole purview of the lending staff.

A mismatch of strategy and culture can significantly elevate risk. Delegating development of a new business to a third-level manager in a personality-driven culture will fail. So will expecting lower-level employees to call the bank's whistle-blower hot line in a CEO-dominated bank.

An initiative to develop fee-based businesses typically fails to account for the differences in the cultures of those businesses as compared to the traditional community bank model. The management team must honestly assess its shared values and beliefs to maximize the opportunity for strategic success.

- **Operating a solid bank takes skill, dedication and effort.**

Matching the leadership, management and staff to the strategy and culture is essential for success. The board's annual assessment of the chief executive should include the CEO's ability to attract and retain a team capable of implementing the strategy within the agreed-upon culture.

Leaders, managers and staff need to "go to work" every day. "Going to work" does not necessarily imply a sober culture. It does require that everyone understands the bank's strategic direction, knows how their skills, motivations and behaviors contribute to achieving the strategy and has confidence that their contribution will be rewarded.

• **A risk oversight discipline will always be required.**

Experienced bankers have had an intuitive sense of the balance between risk and return across the various dimensions of risk.

Enterprise risk management replaces this traditional understanding with more explicit (and quantitative) documentation of a bank's risk appetite and risk assessment. Implementing this discipline at the board level is crucial.

Many boards regret that they did not clearly understand the risks that their management team assumed. Board members need to ask management (and expect informed answers) to the question: "If this action does not work, then what will we do?"

• **Board members have to apply themselves as well.**

Confusion around the appropriate role of the board remains despite the best efforts of the banking associations and groups such as the American Association of Bank Directors to help educate board members. The days of joining a bank board for the local prestige and simply showing up for board meetings have long passed. The new imperative will be investing significant time and effort in board meetings and outside individual development initiatives.

There really is nothing new in all of this. A focused strategy, executed by engaged, committed members of the board, management and staff in a culture that supports taking measured risk, sets the stage for success. The new world of banking will continue to be difficult, but it will also be capable of providing deep satisfaction in the delivery of products and services that support the communities in which we operate ■

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