ABA BANK DIRECTORS BRIEFING

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EDITORIAL: 212-620-7219 SCOCHEO@SBPUB.COM
CIRCULATION: 800-895-4389 JEBERLY@SB-REB.COM

THE DIRECTOR'S JOB

HOW TO SUCCEED–AND HOW TO FLOP–WHEN BOARD MEMBERS TAKE ON THE SALES ROLE

Bankers often look to their board members to help bring in business. But there are successful ways and not-so-successful ways of doing this. And, "bank director efforts to refer business to their banks do not always turn out so well," according to bank directorship expert David Baris.

Baris believes strongly that formal director sales and referral programs, complete with written goals and tracking, produce more meaningful results than do informal, unwritten efforts. A formal program's measurements permit evaluation of whether the overall program, and individual directors' results, produce sufficient return, Baris says.

Furthermore, Baris believes directors ought to be able to earn incentives of some kind for their efforts. However, he added, surveys by the American Association of Bank Directors indicate that while 85% of banking institutions surveyed expect their directors and trustees to generate new business, only one in ten of those banks reward or recognize board members for producing.

"We think there is a disconnect there," says Baris, who serves as executive director of the American Association of Bank Directors, *www.aabd.org*.

"Some directors will be motivated without any incentive," Baris admitted. The reasons include pride of ownership; sense of responsibility; and desire that the bank succeed. But he believes banks that rely solely on such motivation miss potential gains.

Baris was one of the speakers during last fall's ABA America's Community Bankers Council/*ABA Bank Directors Briefing* telephone briefing, "Boards That Sell!: How

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DEAR DIRECTOR:

Amid A Tide Of Pessimism, Some Observers Find A Bit Of Hope Recession Won't Arrive

What if they gave a recession and nobody came?

Boiled down, that's the argument of bank stock analyst Richard Bove in his January 14 report, "Is It Really That Bad?"

It comes at the same time that ABA's Economics Advisory Committee, consisting of leading bank economists from around the country, issued its consensus economic forecast and conditions report. And in the same period when the Administration is calling for a national economic stimulus program; the cleanup of the subprime and exotic mortgage mess is proceeding; and the Federal Reserve Board, ahead of some expectations, cut its key rates by three-quarters of a percentage point.

In taking its action ahead of its regularly scheduled meeting, the Fed's Federal Open Market Committee said it:

"...took this action in view of a weakening of the economic outlook and increasing downside risks to growth. While strains in short-term funding markets have eased somewhat, broader financial market conditions have continued to deteriorate and credit has tightened further for some businesses and households. Moreover, incoming information indicates a deepening of the housing contraction as well as some softening in labor markets."

"Pundits seem to be outdoing each other in their dire predictions"

Is this ride necessary?

Bove, a veteran analyst, at Punk, Ziegel & Company, New York, is no cockeyed optimist. Indeed, he called much of the current trouble in financial services long ago, and expected problems to come home to roost. He anticipated a shakeout—but not a cataclysm. But Bove believes that the country is being "talked into a recession," to use his words, and not one that the nation really has to go through to allow the financial system to purge itself.

Pundits seem to be outdoing each other in their dire predictions, and Bove complained in his report that not only Democrats, but key figures in the Administration, and even at the Federal Reserve, instead of talking things up, are only adding to the momentum towards crisis:

"Not only is there a juggernaut taking every opportunity to frighten the American business person and the American consumer so that they will stop spending, but there is a level of intellectual bankruptcy which is completely unnerving. Consumers are listening. They are spending less. Business people are listening; they are becoming more defensive. The naysayers may get what they want. They may get a recession."

Elaborating, Bove explains:

"I am not arguing that there are no serious problems. ... I am arguing that these problems are being magnified by hysterics in the government and the media. Further, I am arguing that if they keep this up without pointing out any of the positives in this economy, they will drive this country into recession. It is time that these so-called pundits

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"It's time they started building confidence in this economy and stopped trying to destroy it"

started building confidence in this economy and stopped trying to destroy it."

In his report, Bove acknowledges that bank earnings will suffer in the period ahead. But he adds, "It is inevitable that the earnings will recover unless one has become so enamored of the Cassandras that one believes the United States economy is finished." He also noted that banks do best coming out of a down cycle.

ABA committee consensus view

On Jan. 18, the ABA Economic Advisory Committee (EAC)issued its consensus forecast for the economy, which is put together after the bank economists meet with Fed members.

Overall, the group stated that the nation's growth of output and employment will be well below trend for 2008. However, the economists believe that there will be "a noticeable pickup in the second half."

The consensus is that real economic growth will slow to 1.25% in the first six months, rising to a rate of 2.25% in the second half. The group forecasts a moderate rise in the unemployment rate to 5.3% through yearend, versus 4.8% at the end of 2007.

"The risk of substantially weaker economic performance is significant and the EAC now places the probability of recession close to 50%," the committee stated.

"The drag from residential investment will continue to weigh the economy down, but we expect this to moderate after mid-year," said Peter Hooper, EAC chairman and chief economist at Deutsche Bank Securities. "Fed rate cuts and a possible fiscal stimulus package should support stronger economic growth in the second half of 2008."

Hooper said the Fed rate cuts—which turned out to be higher and sooner than the committee anticipated—"are justified because of the continuing turmoil in the financial markets and a weakening economy. Inflation risks increasingly are in the background for now."

Committee's regional scan

In addition to its national work, the committee also puts together its *Regional Economic Outlook*. The latest report indicated that most states saw decelerating growth during the last six months of 2007.

"The economic slowdown varied by region," the report states, "but was largely due to declines to the housing sector and slowing in manufacturing. Most states reported job gains, but gains were not nearly as robust as earlier in the year and many states experienced increasing unemployment."

The 30-page regional report, with quite detailed sections on many states, indicates many local factors influencing each area's current performance and future outlook.

"The challenges to the housing and mortgage market are the most severe in states that experienced extreme price appreciation," the regional report stated. "Following such large price run-ups, western states in particular have hefty inventories of unsold new and existing homes. These inventories have left the housing market stagnant as buyers wait for the market to bottom. Additionally, the payment shocks experienced by holders of resetting mortgages have caused delinquency and foreclosure rates to rise. The expectation is for the housing market to bottom around the end of the year, as home sales rebound and the problematic two- and three-year hybrid mortgages pass reset dates."

One bright spot revealed by the group's regional research is that many areas that benefit from tourism have been seeing a boost from the weakness of the dollar. With the dollar making foreign vacations more expensive, after exchange rates are applied, Americans are tending to "discover America." However, this impact is balanced somewhat by higher energy prices, the report points out.

ABA comments on switching OTS thrifts to call report system

Because of the inevitable conversion costs that savings associations would face, a clear business case must be made before the Office of Thrift Supervision changes the way that OTS thrifts report their financial results and related records.

Currently, savings associations supervised by OTS file the "TFR," the Thrift Financial Report, with the agency. On the other hand, institutions supervised by the Comptroller's Office, the Federal Reserve, and FDIC file the "Consolidated Report of Condition and Income," commonly referred to as the "call report." The two forms differ in key respects. The TFR, for instance, requires much more information regarding mortgage lending and related interest-rate-risk measurement, reflecting the savings association industry's longtime concentration in that area.

The OTS, in a November 2007 Advance Notice of Proposed Rulemaking, suggested that switching OTS thrifts to a version of the call report would reduce their reporting costs and make it easier for their managers to compare results to commercial banks' numbers.

OTS asked for input on the process to be used to evaluate such a proposal, not directly on the concept. ABA noted that comparability to bank documents is something that some savings associations have expressed interest in, when they have diversified beyond traditional business lines. It also noted that some portions of the TFR are considered very time consuming and cumbersome to complete.

ABA also asked that special attention be paid to mutual savings institutions' unique nature, so that their numbers can be compared to peers'. Mutuals' earnings, for instance, may be lower than comparably sized commercial banks, ABA stated, because they often pay more on deposits, charge less on loans, and often donate to charitable foundations that they set up for the public good. ABA also reflected on concerns that any consolidation of reporting schemes could support those that want to merge OTS functions into other agencies.

In addition, some areas enjoy some boost from special factors. For instance, Mississippi, the report notes, "continues to generate something of a growth premium through residual post-Katrina recovery. However, those gains accrue primarily to the coastal regions." Another example is Pennsylvania, which has enjoyed some growth as residents of Maryland, New Jersey, and New York migrate in search of affordable housing.

Manufacturing activity is dragging in many states, according to the report, and while Michigan is hardest hit by the ongoing troubles of the automakers, other states that host large auto plants are going through their own, related troubles.

[Those interested in the full committee statement and links to all the supporting reports will find them at *www.aba.com/Press+Room/011808Economists.htm*]

Mortgage cleanup continues

In the course of its national statement, the ABA committee stated that continued housing sector troubles, the weakening economy, and turmoil in financial markets, were causing many banks to become much more cautious about lending.

Chairman Peter Hooper commented: "Even as securitization has dried up, bank credit is still flowing. Borrowers are rediscovering that the banking industry is well-positioned to meet their funding needs. Underwriting standards will naturally reflect the weakening economy, but creditworthy borrowers will continue to have access to credit."

On a number of fronts, the effort to address the many homeowners in trouble, or facing trouble, as a result of resetting adjustable mortgages continues. Some larger companies have struck agreements with officials in some states, and the national effort put together with federal government involvement continues. FDIC Chairman Sheila Bair, who pushed for

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Directors Can Develop New Business." (To order a CD, go to *www.aba.com/teleweb/tb111407.htm*.)

A FRAMEWORK TO BUILD UPON

Besides providing incentives for successful, or, at least, the most successful board members, Baris said the bank that wants to tap the potential of its board must consider six key points:

1. *Educate board members about the bank's services*, so they understand what the bank offers that can address prospective customers' needs.

2. *Support in all ways possible board members' efforts to identify and reach out to prospective customers.* Business cards for directors and other supporting materials are among the tools some banks make available.

3. *Provide clear direction regarding to whom various types of business or expressed interest should be referred.*

4. *Specify how far the bank feels the director should go in discussing specific business possibilities with customers or prospective customers.* Some banks may feel nothing but general statements ought to be made, for instance.

5. *Provide feedback to each board member.* How else are directors and trustees to know if what they've been referring to bank staff is useful, or just a distraction and waste of time that would be better spent on something else?

6. *Adopt a tracking system.* Some banks make this a focal point of board meetings, to encourage those who don't try to talk up the bank to get on the stick.

"DO'S" FOR DIRECTORS

Baris began his list of "do's" with a story. A director he'd heard of told a prospective client very enthusiastically about a hot new banking product that was perfect for the company.

"Unfortunately," said Baris, "he was describing the unique product offered only by the bank's main *competitor*."

This leads into his first point.

1. *Do learn about the bank's products and services.* Board members can't sell products without knowing what they are.

2. *Do believe in the value of the products offered by the bank.* "You can't sell unless you have confidence in the bank's products and services and enthusiasm about them," said Baris.

3. *Do rehearse what you say to prospective bank customers.* Baris warned directors not to "wing it" when they decide to meet with a prospective customer. Boning up on what the company does or what the individual customer may need, in advance, will help board members make sure they know about the appropriate products that the bank offers, or the right employees to send them to.

4. *Do prioritize prospective bank customers, based on your existing contacts.* Baris suggested going through one's Rolodex and flagging those community contacts which are "yeses" for business and which aren't likely prospects. After that broad review, the board member can categorize them by the services they would likely need.

5. *Do allot a certain amount of time each week to devote in generating business for the bank.* "Even if it's only an hour or two a week," said Baris, "put that time aside."

6. *Do present yourself at all times in a professional manner.* "You'll be representing the bank, not yourself," said Baris. "The reputation of the bank depends largely on you, other directors, officers, and employees. So how you present yourself is key."

Regarding expenses—lunch or otherwise—Baris recommends that if the purpose was bank business, the board member should pick up the tab on the bank's behalf. Likewise, more elaborate efforts such as a golf outing ought to be paid for.

"These can all be legitimate expenses," said Baris, "if they've been considered by the bank and a decision has been made authorizing them."

7. *Do follow the bank's procedures regarding referring business to the party identified by the bank as your contact.* Depending on what's involved, the contact might be the CEO, or it might be the chief lender. But always stick to the plan.

8. *Do cooperate with bank management in any follow-up to the initial contact.* Selling often takes multiple contacts, requiring patience and ongoing commitment to work with staff to win

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something along the lines of the program of the HOPE NOW coalition—ABA is a member—outlined in an earlier issue, said in a recent speech that not enough was happening quickly enough. Bair predicted that if industry efforts fail to slow down foreclosures, there is potential for more governmental involvement.

Now that Senate Banking Committee Chairman Chris Dodd (D.-Conn.) has dropped his long-shot bid for the Democratic presidential nomination, the committee is expected to increase its attention to pending legislation dealing with the subprime crisis. Key efforts have already passed the House, and banks will be watching as the Senate takes its turn.

In mid-January, HOPE NOW reported that servicers assisted 370,000 homeowners to avoid default, through establishment of formal repayment plans or through modification of loan terms. The HOPE NOW "fast-track" program was unveiled in early December 2007, so it was not available for most of that period. Later reports will reflect more usage of the program.

Sincerely,
Steve Cocheo
for *ABA Banking Journal*

Mark Your Calendar: 2008 Board Telephone Briefings Set

ABA's America's Community Bankers Council presents the fourth season of director telephone briefings in 2008, in cooperation with *ABA Bank Directors Briefing.*

April 16: *Directors and the Bank's Portfolios: Understanding Bank Investments and Asset/Liability Management*, Program 13746: Especially recommended for new and intermediate-level directors and trustees, and those coming up for rotation on the investment policy or asset-liability management committee.

July 9: *Board Self-Evaluation And Performance Improvement*, Program 13747: Recommended for veteran boards with little recent turnover; de novo bank boards looking to "refresh and reboot"; and any directors desiring to improve their game.

Sept. 24: *Board Meetings 102: Better Governance For Challenging Times*, Program 13748: For all boards that want better meetings—but not longer ones.

Dec. 10: *Effective Board Committees: The Audit Committee and Beyond*, Program 13749: Recommended for all boards.

All sessions are on Wednesdays, 2:00 p.m.-3:30 p.m. ET. Further details and registration information will be published later this month on www.aba.com

the prospect's business.

9. *Do advise the bank of any positive or negative information that you are aware of about the customer.*

"Your first loyalty is to the bank, not to your friend or to your relative, or to your business associate," says Baris. "If you are aware of facts that are material to the bank in deciding whether to approve a credit, for example, then you need to disclose that information to the bank." For board members with special situations–they may be CPAs or lawyers with a client relationship involved–special issues may arise.

10. *Do be active in community, charitable, and business circles.* "This is how you develop new contacts and renew old ones," Baris said.

DON'T'S FOR DIRECTORS

The very first "don't" offered by Baris was a major one:

1. *Don't promise a prospective bank customer that his or her loan application will be approved.*

This happens too frequently, Baris said. Board members must make it clear to the customer that his or her application will be treated like everyone else's. Promising more than a fair and impartial hearing, he said, "can only cause disappointment and bitterness."

2. *Don't assist a prospective customer in preparing a loan application.* The director's job is to refer business, and follow up if bank staff requests that effort. Beyond that, fingers out.

3. *Don't put pressure on bank management to approve a loan to someone you had introduced to the bank.* "Leave it up to the professional lending staff," said Baris, "and let them adhere to loan policy and procedures."

4. *Don't say anything derogatory about the bank, its management, or the board to a prospect.* This may come as a surprise, but "we've heard about this from time to time," he said.

5. *Don't say anything bad about a bank competitor.* Baris said it is preferable to talk up your institution.

6. *Don't receive any remuneration from a customer, or a prospective customer, that's not fully disclosed prior to the bank entering into any transaction.* "You need to disclose any compensation you've received, or will receive," said Baris, say, from a customer of your own business. But if the compensation is for making the referral or doing work in connection with the loan application, warned Baris, "that can be construed as a criminal violation and *clearly* must be avoided."

7. *Don't withhold any information from the bank relating to any actual or apparent conflicts.* The board member should also abstain from approving the loan or other transaction.

8. *Don't assume, or appear as if you are assuming, the role of a bank lender or other line officer of the bank.* "Make it clear to the customer that you do not have any individual authority to approve any loan," said Baris.

9. *Don't exaggerate or misrepresent the bank's offerings.* Baris said overstating things creates disappointment.

10. *Don't badmouth the bank to the prospective customer if the bank chooses not to approve the loan.* Typically, such a director, after a referred prospect's loan is denied, will make negative remarks about management.

"This shouldn't happen," said Baris.

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