



## Security First National Bank

Non S-Corp bank between \$100 million and \$3 billion



Mike Brewer, president

# A world apart, in more ways than one

Security First is one of those banks that does well in a very modest economy. And it does well consistently. The three-county area of southeastern Oklahoma near the Texas and Arkansas borders is the poorest area of the state. Yet things are not as bad there now as in some other parts of the country. Unemployment, at about 6%, is well below the national average.

“We’re down here by ourselves and don’t feel the big spikes of other parts of the country,” says Mike Brewer, president of Security First, the only “standalone bank,” as he puts it, in the town of Hugo, Okla., pop. 5,500. Brewer says the area is fairly diversified economically, with some broiler (chicken) and cattle farms, as well as an International Paper plant and the headquarters of the Choctaw Nation nearby.

The bank ranked number one this year in non-Subchapter S banks over \$100 million in assets with a yearend 2008 return on average equity of 29.89%. The year before, the bank was number three even though its ROAE was 32.95%. It was number two in 2006, at 33.29%.

### Fit ‘em and hold ‘em

The bulk of the bank’s \$68 billion in loans are 1-4 family residential mortgages (some of them classified as ag loans in call report data). They have some ag production loans to chicken and cattle producers, but few commercial loans, and few auto loans. The mortgage portfolio has been growing steadily for the last 25 years, says Brewer who has been with the bank for 36 years.

A few years ago, many of the top performers were banks that specialized in real estate lending. Often these banks were high-volume specialists. Security First is not of that ilk. It custom fits its mortgages to customers, carefully weighs the risk, makes sure it is compensated for it, gives great service, and holds the loans.

The bank never made subprime loans, says Brewer. It does grade potential borrowers into A, B, C, D categories, and particularly likes “a good B- or C+ risk,” according to Brewer. That’s because the As usually are rate shoppers, whereas the Bs and Cs pay a little more.

The majority of the bank’s mortgage loans are 15-20 year adjustables that adjust every three years. None are sold.

That flies in the face of what most people in the business say about mortgage lending—that it’s a high-volume, commodity business requiring an active secondary market. Much of it is (or

was), of course, but Security First has managed to grow both sides of its balance sheet for many years without being squeezed on either side. It grew from \$55 million in assets in 1995 to \$105 million today.

Funding to a large degree comes from municipal deposits—mainly DDAs—allowing the bank to enjoy a generous net interest margin (6.22% at yearend). Brewer says that “our spread is shrinking like everybody’s,” as adjustables reset lower.

Brewer also points out that the bank doesn’t have any loan losses at present. It has nonperformers, and has had a few foreclosures, but it doesn’t suffer any loss on these because, he says, “we’re collateral lenders.” And, as noted earlier, the bank’s market has been less affected by the national turnaround.



### Buy their lunch vs. eat their lunch

All the above is more the technical side of the story, which is important, but misses the bank’s basic approach to business. Simply put, the bank and all its 35 employees care about the customers. Many businesses say that, of

course, but Security First backs it up.

It has a 15 minute rule, for example. An employee must return a customer’s phone message within 15 minutes. As a result, says Brewer, when customers are weighing options (there are branches of two larger banks in town), they’ll say, “I know I’ll get a call back from Security.”

Here’s another example: When Brewer spots a customer in a local coffee shop, he will sometimes tell the waitress, “I’ll pick up that tab.”

“Customers really appreciate things like that,” he says.

Security First’s service charges are a little higher, though competitive. “But,” says Brewer, “we provide the service.”

This applies very much to the bank’s mortgage lending. Its loan officers make loans that fit the person’s budget. As a result it doesn’t have set rates. The lenders put their heads together, assess the risk, and offer a rate that is fair, but also fairly compensates the bank. Brewer says the approach is similar to retailers who make suits to order.

Hugo, Okla., may be off the beaten path, but these days no place is out of touch with competitive offerings. Security First’s good-service, custom-tailored approach clearly works. Says Brewer, “Customers tell us, ‘You’re a little high, but I trust you’.”

— Bill Streeter, editor-in-chief



**People's Bank of Seneca**

Non S-corp bank under \$100 million



Deron Burr, president

# A good time to be a community bank

**B**ankers Deron Burr and John Klute were talking at lunch recently in Seneca, Mo., about local economic conditions, when Klute observed how interesting it is that many people in town “ask us how *we’re* doing,” referring to People’s Bank of Seneca, where they both work. Usually it’s the other way around.

But times are not normal, and in Seneca, a town of 2,135 on the Oklahoma border, 16 miles south of Joplin, Mo., people want to know how their bank is doing.

The answer is: Quite well.

The \$75 million assets People’s Bank of Seneca had the sixth-highest return on equity (19.53%) among banks and savings institutions under \$100 million in assets that are not subchapter S banks. It is the only hometown bank in the community,

up against a branch of a large bank, and is a very active and visible supporter of the community. But such is the effect of relentless headlines about banking troubles, that people have become the questioners of the bank.

There’s another reason for the questions, says Burr, who is the bank’s president and CEO. They know how important the bank is to the community and figure if we’re still lending, then the community is okay.

They *are* lending.

“Loan demand is pretty decent,” says Burr, “though I’m not going to say it’s great—construction has declined.” Primarily a retail bank, People’s does a “little bit of everything” in terms of loans, including non-conventional mortgages. “That’s one place community banks have an advantage,” he says, “we know people and can structure [a loan] where we’re comfortable.”

### School contest leads to a 3% account

Comfort works both ways, and Burr says that with all that’s transpired in the last 9 to 12 months, people feel more comfortable dealing with the local bank they know. In the case of People’s Bank’s 16 employees, they are “known” quite literally.

Many of them, for example, attended the recent graduation ceremony at Seneca High School, even though they didn’t necessarily have any children in the school. It’s just a big event in the community, explains Burr.

He’s the radio announcer for the high school football games, which in this part of the world are a very big deal. Most of the bank’s employees help work the games.

People’s Bank adopted another bank’s idea for a “Millionaire

for a Day” contest and built it into a major event, which led to the creation of a new deposit product.

In the contest, middle school students are asked to write an essay about what they would do if they had a million dollars for a day. In front of a full assembly with the bank’s entire board present, the winners are honored and given a check for the amount of the interest earned on a million dollars in one a day.

With passbook savings rates in the 1%-1.5% range, Burr says he felt they needed to make the winners’ checks a little larger, so they came up with a 3% passbook account.

They don’t advertise it, but when someone calls for a CD rate, the bank mentions the passbook account. Not surprisingly, it has proven popular. People drive down from Joplin to deposit \$50,000 to \$70,000 in the bank, says Burr. He and his board monitor the product closely. “If we had an influx of money, we’d have to adjust the rate,” says Burr. “We tell people that’s a possibility when they sign up for it.”

As long as the bank is able to make a decent margin, it will continue with the passbook account, says Burr. At yearend, People’s net interest margin stood at 7.03% and loans grew 34%.

“In this economy, people are getting back to basics,” says Burr, “and that includes the old, plain Jane savings account.”

In addition to that source of funds, People’s Bank has another stable source that is a bit unusual.

The bank is majority owned by The Eastern Shawnee Tribe. One of the initial investors in the bank in 1996, the tribe owns several businesses besides the bank, including two casinos. The latter generate a lot of cash, some of which ends up as deposits.

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### Many hats, zero turnover

Burr says the bank’s efficiency ratio of 47% results from two things. First, it has had zero turnover for more than three years. *None*. “So we’re not spending time training someone new,” he says, “and over time people get more efficient at what they do.”

The second thing is typical of many community banks: everybody does more than one job. Burr says most people like wearing multiple hats because that way they don’t have to do the same thing every day.

He expects this year to be similar to the previous two years.

“Consistency is the goal,” he says. “We’ve been very aggressive the last two to three years in identifying potential problems and addressing them sooner rather than later.”

— Bill Streeter



## Home Bank of California

S-corp bank over \$100 million



# With CRE credit, Home Bank prospers

If you went by general trends and conventional wisdom, Home Bank of California should be on life support—not gracing a spot among the top 25 institutions in its class.

First off, virtually every loan in the \$149.8 million-assets bank's portfolio is a real-estate credit. The vast majority of those loans are commercial real estate loans. Not business loans that happen to be secured by commercial real estate, but real, honest-to-goodness loans made on income-producing property. And the remainder that isn't CRE consists of construction loans and multifamily and single-family mortgages. The bank doesn't have any C&I loans and is only beginning to raise deposits through noninterest-bearing demand accounts.

And yet the bank manages to have exactly one piece of OREO, a bed and breakfast that didn't catch on. And its yearend 2008 ratio of nonperforming loans to total loans was

0.43%—though Byron B. Webb III, president and chairman, admits that a couple of loans are giving management a fit or two.

As a result, the family-owned S corp bank has produced a very consistent return for its shareholders, ranging between 29% and nearly 36% in the last four years, hitting 31.73% in 2008.

### Atypical state-chartered roots

Webb, 48, is the third generation of his family to work in banking. His father started Home Bank in San Diego's middle-class Pacific Beach area as an uninsured state-chartered thrift and loan association in 1981. The bank became FDIC insured in 1985 and eventually changed its name to Home Bank of California.

Through all of that time, and until the end of 2007, the company maintained the thrift and loan charter. As a thrift and loan, Home Bank could not accept demand deposits, so its funds gathering was limited chiefly to time deposits, and Federal Home Loan Bank advances. Webb explains that this structure favored finding higher-paying credits, such as commercial real estate loans, to make up for the higher-cost funding base.

In late 2007 the company changed to a commercial bank charter, to expand its funding mix further. Webb says that the effort to raise checking deposits remains in its early stages.

At present, the bank's borrower base and depositor base have almost no overlap at all. Deposits are chiefly local, and can be readily raised in the highly competitive market so long as the bank is willing to pay consumers the going rate or better. The bank is currently exploring two national rate listing services as well as the ABA-endorsed CDARS program.

Building up a commercial deposit base will take time, as many

borrowers don't come from the bank's immediate geographic vicinity, and those that do generally think of Home Bank strictly as a credit source.

### Making CRE perform

What's the secret ingredient, the special factor at Home Bank? There isn't one actually.

Home Bank doesn't emphasize any particular type of property, nor does it avoid any specific type of CRE loan. With appropriate due diligence, it will even do gas stations.

But you won't find Donald Trump or his ilk coming to Home Bank for credit.

"We're not even on his radar," says Webb, and you won't find the Fortune 500 on the bank's customer list.

The typical borrower is a business person who owns two or three small- to medium-sized investment properties. They generally either want to buy an additional property on credit, or they wish to access equity in their existing holdings. Most of the bank's clientele initially come to it through connections made by commercial mortgage brokers. Anything within a two-hour drive is considered within the bank's footprint.

### Know the property. Cold

"Our philosophy has always been to be debt-service driven," says Webb. The bank won't make a loan on a property where the deal can't support itself.

Webb says that his father, who died in late 2008, had an unmovable, unchangeable part to his credit *modus operandi*. "He wanted to see that the property would pay the loan," says Webb.

Webb himself inherited a healthy amount of that skepticism. Before coming back to run the family business in 2003, he spent some time with a large savings institution in its credit area. He says he kept seeing loans that didn't make sense to him. A loan broker who sold to this institution finally told him, "Ride the wave." Everyone was enjoying the surge, and profiting from it, weren't they?

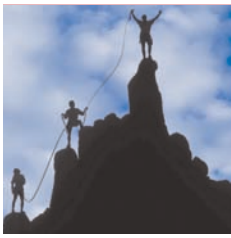
Webb decided he wanted to work elsewhere.

Things are different at Home Bank.

"It's our longstanding philosophy that every piece of property that we make a loan on is physically inspected by somebody from the bank."

Sometimes it's a loan officer, sometimes it might be Webb





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himself. Whoever makes the trip looks over the building, takes pictures, and checks out the neighborhood. How many other “For sale” or “For rent” signs, for example, can they spot on nearby commercial buildings?

“Before we even ask for them to spend money on an appraisal,” says Webb, “we want to speak rationally with them. We want to pretty much know in advance where we are going to be.” He says a key challenge of commercial real estate credit is getting past the often-enthusiastic applicant’s pitch. Zeal doesn’t make deal.

In addition, before a loan is granted, just about everyone on the loan platform is going to review the proposal and have some input. Beyond this is the bank’s loan committee, and then there is the final word: Either Webb or the bank’s EVP

must approve the loan, personally.

### Adjusting for fit

Over the years, much lip service has been paid to credit quality, but some banks that have bought the music haven’t always danced to the tune when circumstances changed. That’s something that sets Home Bank apart. The privately held company actually shrunk its asset size in 2006 (by 3.5%), 2007 (7.6%), and 2008 (1.6%)—something a public company would have difficulty with, at least in the absence of a regulatory order.

Webb explains that sticking to the bank’s credit standards means walking away from deals. In recent years, he says, “there were a lot of loans out there, but they didn’t make sense to us. We are not willing to take an unnecessary risk.”

Naturally this hasn’t always been a

crowd-pleaser, Webb admits.

“It’s hard to get people to understand that their office building doesn’t necessarily merit the same treatment that their house does,” says Webb.

Home Bank has seen some improvements in commercial markets in recent months, and Webb believes the days of shrinkage are over. The bank’s first four months of 2009 indicate that this will be a growth year for the CRE portfolio.

“I anticipate we’ll have some good growth this year,” says Webb.

One question that may be running through your head, after all the CRE talk. Given the bank’s business mix, why “Home” Bank?

“My father liked the name ‘Home,’” says Webb, “and, since it was his company, he got naming rights.”

—Steve Cocheo, executive editor

## Bank of Dade

S corp bank under \$100 million

# Tri-state market and cost control build success

Interstate 59, built to connect Chattanooga, Tenn., to Slidell, La., passes through the very northwest corner of Georgia for the duration of three exits.

In its own way, Bank of Dade, in Trenton, Ga., is also a connector. The \$88.2 million-assets bank does business in Alabama, Georgia, and Tennessee, and is in a bedroom community for Chattanooga.

“We deal in all three states, and the laws are different in each state,” says Mike Tate, president. While keeping up with three states’ rules is a challenge, it’s generally not been a compliance weakness, Tate adds.

Georgia banks generally have taken a PR drubbing this year and last, damned by association with the significant troubles, especially involving some de novos, out of the Atlanta region. But Georgia is much more than Atlanta. Bank of Dade placed third by ROE (36.84%) in its category, up from fifth in the 2007 rankings. (The bank has done well in past rankings, too, though these are not directly comparable, due to differences in past treatment of S-corp banks.)

Tate attributes the bank’s success to getting many basics right. Two outstanding factors are: expertise due to staff longevity and cost control.

Regarding longevity, Tate serves as an example himself—he’s been with the bank for more than 33 years—and the bank’s senior loan officer has been there about 40 years.

On the expense side, Tate saves wherever he can. For example, he’s been stressing webinars and similar approaches to remote learning in order to cut staff education costs and the associated travel expenses. Internet statements have been adopted, to save on paper and postage. And the bank makes significant use of part-time employees

that it hires directly, avoiding temp agency costs. The recent closure of a large carpet plant in Trenton has freed up many workers for possible part-time employment.

Tate says the bank has also benefited from some good economic breaks in its markets. Tourism is a significant factor. The area is lush with Civil War history, with both the Chickamauga and Lookout Mountain battlefields nearby. And Volkswagen of America recently began construction on a new plant in Chattanooga. The company is investing \$1 billion in the plant, which will make a new VW sedan beginning in 2011, and expects that it will employ 2,000. All told, more than \$272 million in local contracts related to the plant have been announced.

—Steve Cocheo

