
STRATEGIC PLANNING SEASON IS UPON US

Skip the tinsel and concentrate on these essentials

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It is strategic planning season!

And there's a lot of stuff written about it that distracts from the essentials.

Two critical questions you must answer

It seems in the fall of every year, community banks (at least many) decide they need to have their strategic planning session. Some of these are annual (as they should be). Others are every couple of years, and some are every three. Some are outside facilitated. Some are facilitated by an insider (very tough job for the CEO or inside officer). Some are touchy-feely (not the ones I facilitate!) and some simply address the issues, make decisions, and move on.

A common thread through all community banks' strategic planning, however, is this question:

How prepared is the board of directors, with the input from the senior management team, to strategically allocate the bank's financial and managerial capital?

If the board starts with a look at managerial capital, simply because it is easier to assess, the board generally knows the capabilities and whether the bank has underutilized managerial resources.

Financial capital, however, generally takes a little more discussion.

Considering financial capital

The issue of what financial capital does the bank have to work with depends in large part, at least as a starter, with where the bank's Tier 1 leverage ratio is, and where the board wants it to be.

If it is at 11%, and the board is comfortable with 9%, then there is 200 basis points of excess capital on whatever the bank's asset size is. (For example, say the bank is \$300 million and has 200 basis points of excess capital, that is about \$6 million that it could strategically allocate in some fashion.)

Because the regulators are now demanding more capital across the board, for planning purposes, many banks (not all) are assuming that somewhere in the neighborhood of a 9% Tier 1-12% total risk-based is going to be the de facto minimum in the future.

So, the first step in the process is, "let's figure out what capital we have to work with presently." Let's add to that bank earnings less dividends to the holding company for shareholders or debt service or other purposes which would result in net retained earnings. Let's add to that capital that the holding company can generate for the bank either through debt,

equity, or some combination. Once we add that all together, then the board will know what financial capital is available over the next few years.

Allocating financial capital

The issue then becomes how does that capital get allocated strategically?

Should the bank allocate it for organic growth? Or for an acquisition of another bank or a branch?

Should the bank allocate it for the acquisition of another line of business, such as insurance, brokerage, or trust?

Should the bank allocate it toward increasing the cash flow to the shareholders and enhancing shareholders' direct value through that mechanism?

Should the bank holding company allocate that excess capital toward creating liquidity for the shareholders by purchasing holding company shares at a fair price and retiring the shares?

Should the bank holding company allocate that capital for some other strategic purpose not noted above?

Down to the essentials

The real question in this season of strategic planning is, what resources does the bank have to work with, both managerial and financial, and how should they be allocated strategically over the next several years.

That is a good place to start.

About the Author

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