

Survive and Thrive: The Importance of Leadership

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October 1, 2009

"Management is doing things right; leadership is doing the right things." -Peter F. Drucker

During this economic downturn, core assumptions in the financial services marketplace have come into question and the extraordinary uncertainty continues to dominate headlines. Such headlines have largely targeted financial errors that spurred the recession and have contemplated what needs to change to ensure such errors are not repeated. The focus has been less on what has been accomplished with occasional mention of just how important leadership and management are to the continued success of any institution. These indeed are not ordinary times and few predicted the current economic environment. External factors have certainly played a role in present challenges, but they are not the sole cause. We cannot simply wait for asset quality to magically improve and/or earnings to return. Sustainable strategies for long-term profitable growth with leadership that ensures execution remain the key determinants.

We dare not let the headlines blur what is reality for many! Community banks remain the backbone of this industry and of the communities wherein they reside. The second quarter FDIC *Quarterly Banking Profile* demonstrates that community banks outperformed the banking industry in several key areas:

- A higher percentage of community banks were profitable in the second quarter compared to the industry overall. Specifically, in the Midwest, 23% were unprofitable compared to 28% nationwide. Likewise, approximately 38% of the banks reported an earnings gain in the Midwest compared to 35% nationwide.
- As of June 30, 2009, credit quality was better at banks with less than \$1 billion in assets, as measured by nonaccruals and OREO to assets.

Over the past year, we have facilitated strategic thinking sessions on all the critical issues—funding, capital raising efforts, cost containment, profit improvement, talent retention, succession planning, and of course, regulatory orders of all kinds that demand immediate attention and require ongoing, fluid strategic solutions. Framing the appropriate issues, identifying potential solutions, incorporating proper alignment, and determining priority recommendations are challenging, especially in an unforgiving and ever-changing environment.

Experience has proven that no matter how well strategy is plotted, the real challenge resides in the actual execution of strategic initiatives. In difficult times, consequential decisions must be made quickly, and many chief executive officers and senior management teams struggle with a true culture of accountability and fostering an internal culture in which open discussion can be had surrounding the "right" possible solutions to the problems at hand. This feat becomes

even more challenging if a culture of accountability is not presently in place and/or has not been the norm.

Responsibility for execution of strategy rests squarely on the shoulders of the chief executive officer and the executive management team with effective governance from the board. In these times, one is well served to periodically reference Section 4.1 – Management in the FDIC's *Risk Management Manual of Examination Policies*, which begins with this important sentence: "The quality of management is probably the single most important element in the successful operation of a bank." We couldn't agree more. In all honesty, there are a number of "troubled" institutions that we feel certain have the management capabilities to weather this storm and have put together a comprehensive plan to do so that is being implemented and executed with both care and speed of urgency. The banks that keep us awake at night are in less serious shape today but likely do not have the leadership and management horsepower to pull through with success over the long haul.

While economic problems in specific markets often play a contributing role in whether an institution is or is not classified as a "troubled" bank, in many cases, the day-to-day manner in which banking business is done ultimately determines a bank's success or failure. While capital is king and asset quality, liquidity, and earnings dominate headlines, competent leadership and management are at a premium and imperative to have in place! With so much emphasis on the loan portfolio, one can easily neglect the most important asset: The leadership at the helm and the employees that follow. In short, what we refer to as the "people portfolio."

It has never been more imperative for the board of directors and the executive management team to have a comprehensive "management plan" in place that will proactively outline the necessary priorities that demonstrate a concerted, communicated effort to urgently assess the current condition of the bank and to outline the appropriate recommendations to improve or sustain performance. All components of this management plan should align with strategies needed. It cannot solely be about asset quality, adequate capital, low-cost deposits, the need for enhanced profit improvement, or potential liquidity stress events. It is about all of those critical issues combined in an executable plan that must be systemically implemented within a well-led culture of accountability.

Key themes to keep top of mind

1. **Timely implementation and execution of priorities, including the potentially painful ones, is a challenge most bankers would prefer to avoid or delay.**
Framing the issues, identifying potential solutions, incorporating proper linkage, and determining priority recommendations are difficult but often enlightening accomplishments. Go for it! Get even better at this!

2. **Community banks must be willing to build the appropriate infrastructure and systems to accommodate prudent, ongoing risk management and accommodate growth.** Without these structures, long-term profitability cannot be sustained, no matter the bank's size. Stated simply, there was too much emphasis on loan growth and sales without the necessary investment in the infrastructure to support it. After all, we operate in a high volume, low margin, and highly leveraged environment. Invest for the long term, even now!
3. **It does not have to be revolutionary.** Leadership has never been more important, and in these circumstances and with so much at risk, it is imperative. Peter Drucker noted that "No institution can possibly survive if it needs geniuses to manage it. It must be organized in such a way as to be able to get along under a leadership composed of average human beings." Many of today's regulatory enforcement actions require the board of directors to ensure an objective assessment of management's capabilities, performance, and capacity. Proactive financial institutions throughout the country are not waiting for the regulators to mandate such but are renewing the commitment to ensure that assessment is ongoing and an integral part of the culture. As we near year-end, ensure that appropriate management assessment is ongoing, aligned with strategy, and executed with full accountability.
4. **It all comes from people.** In the mid 1980s, *In Search of Excellence* began with a short sound bite: "It all comes from people!" Simplistically put, we have found that no matter what the bank issue or problem might be, when stripped to its core, always and somewhere, it has been a management or leadership void.
5. **External factors have played a role.** They are not the sole cause.
6. **The characteristics of a bank's internal culture are vivid descriptors of its health and well being.** Painfully, as some institutions have recently discovered, the culture they thought was in place was not the culture employees described. Take the blinders off and face reality!
7. **Community banking has become increasingly competitive across a broader geographic footprint that defies location for some segments of the bank's existing and prospective customer base.** Continued investments in technology leadership and IT expertise are imperative despite lower earnings. Do not be left behind!

Critical components of a management recovery plan

For the board and executive management team, outside assistance with industry expertise can significantly enhance the strategic thinking process, provide needed objectivity, assist with execution and accountability, and produce a quantifiable return on investment. Ultimately, outside assistance can help with important priorities:

- Asset Quality
- Asset Liability Management
- Board Governance and Board Succession
- Human Capital (Management, Staffing, Organizational Structure Evaluation, and Committee Structure)

- Liquidity, Contingency Funding, Liquidity Stress Testing
- Core Deposit Growth
- Capital Adequacy (potentially raising additional capital)
- Management Assessment
- Profit Improvement Outline
- Realistic Budgets That Align With Variable Compensation
- Risk Management Assessment
- Ongoing Communication Plan(s)

The outlook

Difficult times can be an opportunity in disguise. To survive and thrive, financial institutions must exploit current opportunities—carefully, deliberately, and thoughtfully. At the end of the day and at the core of every story is the quality, capability, performance, and capacity of leadership. Continually enhance leadership at both the board and senior management levels. In doing so, your financial institution will not only survive and thrive, it will be a long-term winner of sustainable shareholder value. Make it happen!

About the Authors

Terry Saber has more than 25 years of experience in the areas of strategic planning, human capital, executive compensation, and executive coaching with family-owned, privately held, and publicly traded financial institutions; state banking associations; and nonprofit organizations. Terry is also nationally known for her facilitation skills as well as her all-inclusive, highly customized, and organization-specific approach to strategic planning and performance management. To learn more, please contact Terry at tsaber@wipfli.com.

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