THE
Board Chair Forum
NEWSLETTER

Opening the door to new ideas

Gerrish Smith Tuck, Consultants and Attorneys
September 2020

In this month's edition of the Board Chair Forum Newsletter, we take a bit of a look at how change is being thrust upon us in all kinds of different ways, including changes for our organizations, as well as changes to our organizations. We highlight some ways that community banks are changing for the better, and highlight some of the difficulties of other changes we may not quite be prepared for.

As you read the Newsletter, we would encourage you to keep in mind that change is inevitable, but the job of the Board Chair, as well as other members of the Board and senior management, is to decide which change is change for the better, which is change just for change's sake, and the types of change that might also be harmful. If you keep in mind the core principle and fiduciary obligation to create and maintain shareholder value, you may find clarity in analyzing those differences. We hope you can take away several things worthwhile from this month's edition.

Happy Reading!

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Board Chair's Summary

- The Change We Knew Was Coming: Branches
- Should You Stop Focusing on Shareholders?
- There is a Changing Focus on True Cost Savings
- How to be Ready for Change
- Is It Ever Too Early to Think About Succession?

The Change We Knew Was Coming: Branches

The demise of the corner branch has long been predicted and has long been inaccurate. But, with the changes we are facing from COVID, a new push toward technology, more remote working and demands for remote access, is change in our branch structure being forced upon us? It seems you cannot go a week without seeing another article about a large or regional bank selling off a host of their branches. Are community banks good buyers for those? Is continuing to invest in real estate and better locations the right way versus investing in better technology?

It seems to us there will always be a need for a local branch in some shape or form. But the point is, the shape and form may look dramatically different. If you think about the types of things that have changed, you will soon realize that banks are probably last in line to change. Our airports and how you check in look different, hotel lobbies and front desks look different, the way our houses of worship are designed now look different, the list goes on and on. However, even new construction of bank facilities, for the most part, looks very similar to the way it did 20, 30 or more years ago, with just updated curtains, carpet, and fewer ashtrays!

While it is true that you do not really need a corner branch to get a loan anymore, it sure seems like people still look for the corner branch to make a deposit, and those core deposits are what create value for your organization. So, yes, we knew change was coming for our branches, and it's here. We are beginning to rethink structure, layout, and now are even relooking at job and work functions in light of the ability to work remotely, hold virtual meetings, and the like. As the larger banks sell their branches, there may be some good opportunities, but keep in mind it may require something more than simply buying the building and its assets and liabilities. It may require an overhaul of a lot more.

Should You Stop Focusing on Shareholders?

Those of you that know our firm well know this is probably a ridiculous question. For years we have constantly preached the necessity of the fundamental philosophy of focusing on shareholder value. But pick up some recent headlines and you will see a renewed emphasis that publicly reporting organizations are limited in their ability to engage in stock repurchase programs to provide liquidity for stockholders. Further, there is a continuing focus on whether dividends are appropriate to be paid at this point in time. Yet, for almost all of our community bank clients across the country, both of those activities continue to be forefront in the minds of boards and management as they seek to find ways to create and return value to shareholders. Even during these times, unless you are extremely thin in capital, an appropriate dividend policy is a must. Likewise, as we have mentioned in previous newsletters, using your bank holding company as a source of liquidity by being the "purchaser of first resort" anytime there are shares available for acquisition, is a win for both the selling shareholder and those shareholders who retain shares and experience increases in earnings per share, return on equity, and other metrics. So, while there seems to be pressure on larger banks to stop focusing on shareholder value, take pride in the fact that most of you are not bound by those same rules and continue to find those shareholder value opportunities where they exist.

There is a Changing Focus on True Cost Savings

We are proponents of the idea that you cannot really save your way to profitability, you must focus on growing the revenue side. However, more and more organizations are now being forced to adopt a kind of change they never thought would be necessary, and that is to make the difficult decisions to generate true and immediate cost savings, sometimes in dramatic fashion. Take, for example, the recent (alleged) merger of equals involving BB&T and SunTrust, now known as "Truist Bank" (insert your own joke here about this made up name). One of their headlines following that transaction was (not shockingly) that the organization would be undertaking something that was described as being a very aggressive branch and personnel rationalization strategy. We will have to admit, that sounds very corporate, formal and docile, but the interpretation is, we are about to close a lot of branches and fire a lot of people. The simple reason is that the organization needs to find substantive, real, true cost savings to make the combined organizations create value for the remaining shareholders.

The same is true in your organization too. We were recently with an organization that made the difficult decision to sell its insurance agency subsidiary, not because they did not have good people working there, not because it did not make a little money for the organization, but the simple fact that it was only marginally helpful. This organization could find tremendous cost savings by selling the subsidiary and redeploy those savings and redirect the assets (some personnel and other items) to more income producing areas within the bank. A difficult decision to make, but one that will bear real fruit in the short term. Again, this does not mean we should necessarily fire a lot of employees and close or sell branches (like the big banks), but it does mean we have to be honest about underperforming locations, non-revenue-generating products and services, and be willing to look for honest, true cost savings through the use of technology or otherwise.

Finally, COVID has also changed the outlook for a lot of Board Chairs and other board members and senior management who now realize that some functions of the Bank can still be adequately performed remotely without the necessity to drive to the local office. As a result, we see that some of those kinds of changes may be more permanent in nature, where we never return to the way it used to be.

How to be Ready for Change

During a recent keynote presentation, we addressed the crowd and asked "Are you ready for the change that is coming?" We then immediately answered the question for the attendees, their organizations and also for ourselves with the answer being a resounding "NO! You are not ready for the change that is coming." The reason we knew that is because we are not ready for the change that is coming either. None of us are really ready – emotionally, structurally, tactically, strategically, and probably a thousand other ways. But, the point to be made is that no organization, no board chair, no board of directors and no management team can truly be prepared for change when we know it is going to be change in unexpected ways. However, what we can be ready for and try to ramp up for is being able to quickly adapt to the pace of change. Having the pieces in place to be able to move quickly when change happens will be a large part of the battle. It does not mean we have to be predictive of every type of change that is going to come our way, but if we are willing to embrace it with an attitude of welcoming the change, and have the personnel and the funding necessary to keep up with the relative pace that the market is forcing upon us, we will all be better served.

Is It Ever Too Early to Think About Succession?

While we are on the subject of change, what about the changes in ownership, changes in your Board, and changes in your management team? These all generally fall within the categories of succession planning. Most organizations have done a pretty good job with management succession over the past decade or so, and more recently the idea of board succession has become more prominent, with many organizations improving that process. But now, we think many organizations are going to be faced with new scenarios of appropriate ownership succession.

Recently, we met with an organization that we think was taking great strides to ensure the longevity of the organization and appropriate succession planning. They were doing that by basically adhering to the concept that it is never too early to start thinking about and planning ownership succession. For example, a family bank that has a tight ownership group of close family members probably needs to already be thinking about the next generation that will be coming up. Would it surprise you to learn that an organization is taking specific steps to get stock in the hands of the next generation of owners, all of whom are less than 30 years old? Furthermore, would you think it is crazy to add men and women who are in their twenties to your Board? For this organization, not only was that a good idea, it was paramount to maintaining independence for years and years to come.

In discussing the reasons behind those actions, it was unique to hear an organization say that while it had the benefits of ownership succession, it took on a much greater role by focusing on what it really means to be an owner in a community bank. What are the responsibilities that come with the job beyond understanding debits and credits? What does it mean to be a leader in your community? As a young person, can you learn the balance of conserving capital versus paying dividends versus asset growth? Why wait until the next generation is in their forties or fifties and then throw them into the Board whenever a seat is vacant, and maybe give them a few shares and hope they figure it out on their own? Learning from an early age and having a mentoring program with other owners is the type of positive change and a new outlook and change for the way of doing business that can benefit all of us.

Meeting Adjourned

Perhaps you have seen the announcements that the Community Banking Chairman's Forum (the actual forum and not the newsletter) has been scheduled for January 14-15, 2021, again in Naples, Florida at the Ritz-Carlton, and it will, in fact, be a live, in-person facilitated discussion by us. We are hoping that many of you by that time will be tired of the snow, the cold, COVID, a crazy college football season, a messed up pro football season, a hoped for conclusion to the Presidential election, and a thousand other reasons to get down to Naples in January to discuss issues with your fellow Board Chairs, and other directors. It is not too early to sign up. You can find out more information at the following link: Community Banking Chairman's Forum.

Also, don't forget about our new YouTube channel also. You can see current videos that we have posted and hear our community bank commentary on other issues of importance. Feel free to go to the channel, subscribe, and "like" the videos. Please use this link: https://www.youtube.com/channel/UC8NUEl2_RDd9Qzc-ZUjUD1g.

We also want to thank many of you for the positive feedback you continue to provide us on our newsletter, including, in particular, the tremendous feedback we received regarding the brief overview of the core steps in an acquisition transaction that we styled, "The Anatomy of a Community Bank Deal." If anyone else would like a copy of that, please reach out to us and we will email it to you.

Until next time,

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