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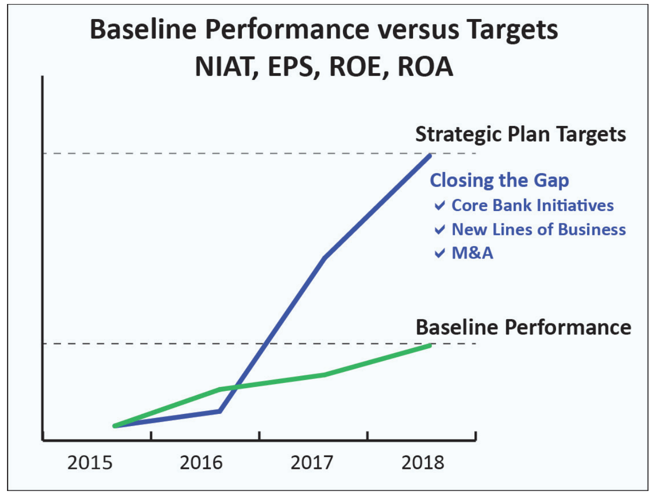
# Baseline Performance Forecasting is a Powerful Strategic Planning Tool

It is well understood that when formulating a strategic plan the executive team sets a future vision for the organization, enumerates the strategic and financial goals that they wish to achieve, and specifies the strategies and initiatives to achieve those goals. A financial forecast can then be developed that encompasses the potential consolidated performance of the bank and measures whether or not the plan attains those goals.

There is a simple but powerful corresponding forecasting exercise that should also occur in the development of the strategic plan. That exercise is to forecast the financial performance of the bank over the plan horizon before considering any changes in strategy or resources. This provides a foundation for understanding the gap in performance between what the bank would achieve ceteris paribus and the financial targets that it aspires to achieve by the end of the plan horizon. This is called the Baseline or Momentum forecast.

The Baseline forecast should be derived from the bank's recent actual financial performance, adjusted to exclude any non-recurring events that would result in a material misrepresentation regarding future performance. In essence, it is the estimation of future financial performance that assumes present trends continue.

The output of the Baseline forecast exercise should consist of the income statement and balance sheet for each year of the planning horizon, the actual and forecasted financial ratios and statistics used by business managers to evaluate financial performance, and documentation detailing the key assumptions underlying the Baseline forecast. The assumptions should be simple and should err on the side of conservatism. It is important to note that the Baseline forecast is not a representation of a bank's annual plan or a representation of performance that the management would present to the board of directors.




Quantifying the differences between baseline financial results and targeted results enables development of specific strategies to close any gap. Without this, financial forecasts and strategies are out of sync.

The Baseline forecast serves as a quantitative foundation upon which strategies can be vetted and prioritized. It enables the executive team to quantify where financial performance must be improved in order to achieve the desired targets. Also, it dimensions the magnitude of the required improvement and therefore helps the executive team to focus on the strategies that will make a material contribution toward closing any shortfall.

# Solving the Small Business Dilemma

*Excerpted from BAI Banking Strategies, March 27, 2015 by Rolland Johannsen and Mary Beth Sullivan.*

Serving small businesses effectively requires business practices, organizational constructs, and value propositions targeted to this particular market segment.

For years banks have recognized that the small business market represents a significant opportunity to drive both balance sheet and earnings growth. The reasons are straightforward:

- The small business market is large and growing. Currently there are over 28 million businesses categorized as "small," representing more than 90% of the total number of businesses in the U.S. Moreover, 500,000 small businesses are created every year.
- Small business relationships can be more profitable on average than most consumer relationships. Deposits can be significant and are concentrated in non-interest bearing accounts while loans tend to carry higher interest rates than larger commercial credits, contributing to attractive margins.
- Small businesses also are strong prospects for a broad range of value-added fee services.
- Small business owners and their employees tend to be attractive consumer customers, offering further growth opportunities.

Despite these compelling reasons to focus on small business as a strategic imperative, success continues to elude many banks that try to achieve meaningful market positions and results with traditional business models and approaches.

### Managing Across Business Lines

The key is to agree on a small business definition that helps scope the size of the market, provide insight into critical customer needs, and build appropriate product and distribution capabilities while maintaining enough flexibility in implementation to accommodate individual customer situations.

For a long time there has been considerable debate on whether small business is a retail or commercial business. Unfortunately, the answer to this debate is "yes;" most small businesses are both,

*continued on back*

# Small Business Dilemma *continued*

which makes it difficult for them to fit within a traditional bank's organizational structures and constructs.

The sales and service model must be managed in a way that cuts horizontally across business lines, rather than within a vertical organizational silo. Successful banks understand this and build their product set and distribution capabilities accordingly.

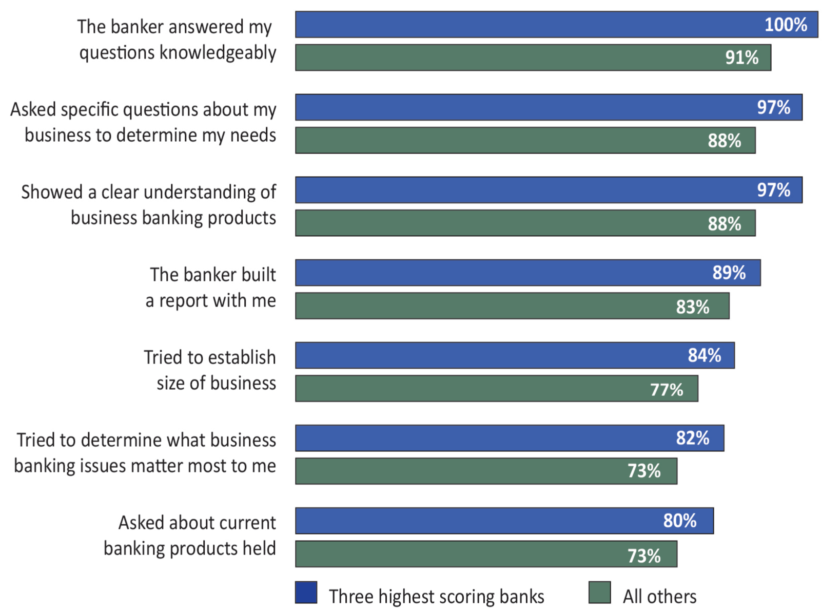
### Easier Access to Credit

Less than 40% of small businesses borrow; even fewer subject themselves to most banks' small business credit processes. Many will use other forms of credit such as home equity loans or even credit cards to provide capital. The use of non-bank, alternative lenders is also growing rapidly.

One of the most important elements of winning in this market is understanding the true nature and scope of the risks involved in small business lending and creating highly streamlined application, decisioning, and funding processes that enables targeted customers to access credit easily and quickly.

Small business remains one of the most potentially lucrative segments in banking. Creating the right business model for the customer is key to winning with this segment.

**What small business owners say are differentiators for leading banks**




Source: ath Power Consulting, ©March 2014.

# CPG Partners with the American Banker to Rank Top Performing Banks

CPG is proud to partner with the American Banker for the ranking of the top performing banks of 2014.

A preview of the rankings of the top 200 public community banks as ranked by three-year average return on average equity is shown below. Overall, 2014 was a good year for the publicly-traded community banks. Median return on average equity was up 14 basis points from 2013 to 2014. This improvement was largely driven by an increase in net interest income levels, which in turn, was a result of growth in loans. Noninterest income levels declined for community banks, year-over-year, highlighting the sector's struggles in boosting fee revenue.

The top 200 public community banks recorded lower expense levels than all public community banks in terms of noninterest expense to average assets. The top 200 were larger, with median assets of $633 million compared to median assets of $409 million for all public community banks. This suggests that the top 200 were able to achieve economies of scale. The top 200 also achieved higher levels of both net interest income and noninterest income as a percentage of average assets. This helped the top 200 to record significantly lower efficiency ratios.

In June, the American Banker Magazine will feature the ranking of banks with assets of between $2 billion and $10 billion. Supporting analytics and a ranking of banks with assets of between $10 billion and $50 billion will also be available online in June.

A ranking of publicly-traded banks with assets of less than $2 billion will appear in the May edition of the American Banker Magazine and is also available online (digital.americanbankermagazine.com).

**Public Banks with Assets of less than $2 Billion[1]**

| Rank | Institution Name | City, State | Total Assets ($000) 2014 | 3-Year Avg ROAE (%) 2012-2014 | ROAE (%) 2014 | Efficiency Ratio (FTE) (%) 2014 | Net Int Income/ Avg Assets (%) 2014 | Noninterest Income/ Avg Assets (%) 2014 | Noninterest Expense/Avg Assets (%) 2014 | Net Loans/ Assets (%) 2014 |
|---|---|---|---|---|---|---|---|---|---|---|
| 1 | Carolina Financial Corporation | Charleston, SC | 1,199,017 | 20.89 | 9.39 | 75.34 | 3.24 | 2.03 | 4.03 | 67.47 |
| 2 | University Bancorp, Inc. | Ann Arbor, MI | 127,922 | 18.75 | 11.46 | 94.39 | 4.09 | 25.00 | 27.52 | 71.07 |
| 3 | First General Bank | Rowland Heights, CA | 585,152 | 16.16 | 15.39 | 35.11 | 4.20 | 0.54 | 1.66 | 85.00 |
| 4 | First Farmers Financial Corporation | Converse, IN | 1,340,000 | 16.06 | 15.14 | 54.65 | 3.64 | 0.79 | 2.52 | 71.89 |
| 5 | Access National Corporation | Reston, VA | 1,052,880 | 16.05 | 14.47 | 60.60 | 3.68 | 2.01 | 3.45 | 76.76 |
| **Median: All Public Community Banks[1]** | | | **408,690** | **6.51** | **6.65** | **72.80** | **3.33** | **0.62** | **3.01** | **67.56** |
| **Change in Median (2013-2014): All Public Community Banks[1]** | | | **25,509** | **0.54** | **0.14** | **0.02** | **0.01** | **(0.06)** | **(0.01)** | **2.17** |
| **Median: Top 200 Public Community Banks[2]** | | | **632,987** | **10.29** | **10.34** | **63.12** | **3.50** | **0.78** | **2.76** | **66.62** |
| **Change in Median (2013-2014): Top 200 Public Community Banks[2]** | | | **51,449** | **3.78** | **(0.04)** | **(0.24)** | **(0.01)** | **(0.03)** | **(0.04)** | **1.12** |

Source: Capital Performance Group analysis of data provided by SNL Financial, LC, 2015. Financial data is based on GAAP filings. If GAAP data was unavailable, regulatory financials were used. Institutions were ranked based on three-year average ROAE from 2012 to 2014. Data are for the twelve months ended 12/31/14, unless otherwise indicated.

1. Publicly-traded bank holding companies, banks, and thrifts with total assets of less than $2 billion as of 12/31/14. Excludes institutions with a leverage ratio of less than 5%, a Tier 1 risk-based capital ratio of less than 6%, or a total risk-based capital ratio of less than 10% as of 12/31/14. Institutions that received a tax benefit of greater than 10% of net income in any year between 2012 and 2014 were excluded. Also excludes industrial banks, nondepository trusts, and institutions that operated as a subchapter S corporation for at least one quarter between 2012 and 2014. Institutions that did not report GAAP or regulatory data at year-end for any year between 2012 and 2014 were also excluded.