Banking's Top Performers, 2008

Part 1: Banks with assets over $3 billion

A year when "ordinary" banking was the new "extraordinary" in terms of positive results. Here's how the best of the large banks came through a tough year

The best thing that most bankers could say about 2008 was that it was over. Not forgotten, but over. Beginning with the collapse of Bear Stearns last March, each month seemed to bring with it some new piece of bad news. By year-end, according to the FDIC, "almost one in four institutions was unprofitable…, and almost two out of every three institutions reported lower full-year earnings than in 2007."

To help address the industry's troubles, the Troubled Asset Relief Program (TARP) was signed into law on October 3rd. Government intervention in the financial services industry has since reached levels not seen in several generations. Nearly 67% of the large public banks and thrifts analyzed this year are either participating in, or approved to participate in, TARP's Capital Purchase Program (CPP; now the Capital Assistance Program). The industry, however, is not out of the woods just yet. We expect that, in 2009, banks will get back to basics, returning attention to core banking businesses and building more relationship-based business models. This year's top 25 public banks and thrifts are, for the most part, institutions that are already implementing these strategies (and most, in fact, have been doing so for several years).

In this first part of the 17th annual *ABA Banking Journal* performance rankings, we review the financial results and strategies of the nation's largest banks and thrifts. Though this piece focuses on top-performing publicly traded institutions, the top-performing private and foreign-owned institutions (and the strategies that they used) may be found at *www.ababj.com.* Part Two of our rankings, which will appear in June, will highlight the top-performing community banks and thrifts of 2008.

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Selection criteria

Our study ranks the performance of domestic publicly held depository institutions with assets over $3 billion as of Dec. 31, 2008. A total of 145 public banks, thrifts, and holding companies qualified under our selection criteria. They were ranked by return on average total equity (ROAE) for 2008. In instances where the reported ROAE was identical for two or more institutions, 2008 return on average total assets (ROAA) was used as a secondary ranking criterion.

Data was provided by SNL Financial LC as of December 2008. Securities and Exchange Commission filings were the source for public company data.

The top performers

In a year where the average ROAE for the pool of analyzed institutions was -4.21%, the strong performance of this year's

Top 25 by 2008 ROE

Public banks & thrifts with total assets of $3 billion or more; data as of 12/31/08. Rankings of all 145 institutions in this category appear on **www.ababj.com**

2009 Rank	2008 Rank	Institution	Total assets (000)	2008 ROAE	2008 ROAA	2008 core ROAE	Noninterest income/ total rev	P/E ratio	Capital ratio	Efficiency ratio	Nonperfor. loans/ total lns
1	2	Bank of Hawaii Corp., Honolulu, HI (bank)	$10,763,475	24.54%	1.84%	21.88%	34.22%	13.77x	12.49%	54.11%	0.22%
2	N/A	Bank of the Ozarks, Little Rock, AR (bank)	3,233,303	15.96	1.15	16.35	17.48	13.72	15.36	41.74	0.76
3	7	Northern Trust Corp., Chicago, IL (bank)	82,053,600	15.57	1.09	13.43	72.17	8.87	15.36	69.39	0.31
4	15	First Financial Bankshares, Abilene, TX (bank)	3,212,385	15.27	1.74	15.07	27.92	22.26	17.04	50.39	0.63
5	10	S&T Bancorp, Indiana, PA (bank)	4,438,368	14.77	1.52	15.11	21.34	15.57	11.82	43.58	1.19
6	3	Westamerica Bancorp., San Rafael, CA (bank)	4,032,934	14.77	1.42	23.54	31.70	18.01	11.76	39.77	0.42
7	29	State Street Corporation, Boston, MA (bank)	173,631,000	14.60	1.12	13.67	72.45	18.21	21.60	72.04	0.00
8	11	TrustCo Bank Corp NY, Glenville, NY (thrift)	3,506,813	14.28	1.00	14.15	15.60	26.42	13.66	51.59	1.54
9	41	NBT Bancorp, Norwich, NY (bank)	5,336,088	14.16	1.11	13.73	26.76	15.53	11.00	54.38	0.66
10	18	CVB Financial Corp., Ontario, CA (bank)	6,649,651	13.75	0.99	13.75	15.10	21.25	15.54	46.78	0.54
11	27	International Bancshares Corp., Laredo, TX (bank)	12,439,341	13.34	1.17	12.92	35.08	11.86	16.35	57.26	2.80
12	17	Cullen/Frost Bankers, San Antonio, TX (bank)	15,034,142	13.11	1.51	13.04	34.84	14.24	12.58	57.03	0.74
13	4	U.S. Bancorp, Minneapolis, MN (bank)	265,912,000	13.05	1.21	14.28	49.77	41.68	14.30	46.74	1.28
14	23	FirstMerit Corp., Akron, OH (bank)	11,100,026	12.76	1.13	11.67	33.29	14.30	11.80	60.25	0.70
15	68	Republic Bancorp, Louisville, KY (bank)	3,939,368	12.58	1.04	16.07	34.30	NM	15.43	56.52	0.49
16	24	Commerce Bancshares, Kansas City, MO (bank)	17,532,447	11.83	1.15	9.92	36.92	18.94	12.31	63.84	0.63
17	26	Glacier Bancorp, Kalispell, MT (bank)	5,553,970	11.63	1.31	12.27	24.37	16.40	15.55	50.05	1.56
18	20	BancFirst Corp., Oklahoma City, OK (bank)	3,867,204	11.33	1.17	9.88	30.75	25.44	13.78	65.06	0.81
19	21	BB&T Corp., Winston-Salem, NC (bank)	152,015,000	11.26	1.11	10.36	40.48	13.46	17.41	51.03	1.43
20	1	TCF Financial Corp., Wayzata, MN (bank)	16,740,357	11.22	0.79	9.63	43.41	17.08	14.65	63.68	1.29
21	34	Hancock Holding Co., Gulfport, MS (bank)	7,167,254	11.18	1.02	10.91	37.40	43.71	11.22	61.22	0.70
22	35	United Bankshares, Charleston, WV (bank)	8,102,091	11.12	1.09	11.90	23.97	21.86	11.00	48.03	0.70
23	6	SVB Financial Group, Santa Clara, CA (bank)	10,020,892	10.93	1.06	12.27	32.36	NM	17.58	57.32	1.54
24	71	Central Bancompany, Jefferson City, MO (bank)	8,962,338	10.70	1.25	NA	34.19	NA	13.67	58.53	1.07
25	87	UMB Financial Corp., Kansas City, MO (bank)	10,976,596	10.51	1.10	9.38	51.13	25.07	14.09	73.17	0.20

Source: SNL Financial LC

top 25 is all the more extraordinary. And yet, most of 2008's top performers generated strong earnings through relatively ordinary banking activities–generating low-cost deposits, making quality loans, and focusing on serving one particular segment extremely well (rather than trying to be all things to all people), all while keeping a sharp eye on noninterest expenses. The similarity between this year's successful strategies and those used in 2007 is no coincidence. Over half of the institutions in this year's top 25 are making a repeat appearance. Many of them remain among the top performers due to strategies that they have adhered to for several years, not just the past 12 months.

Returning to the core–net interest income

Noninterest income may have been essential for reaching the top of the list in 2007; however, in 2008, it was net interest income that mattered. Excluding the more specialized businesses of Northern Trust (#3) and State Street (#7), net interest income accounted for 75% of total revenue at the top 10 institutions and two-thirds of the revenue at this year's top performer, Bank of Hawaii Corp., Honolulu. At 25.54%, Bank of Hawaii's 2008 ROAE was 868 basis points higher than that of the second-place bank, Bank of the Ozarks, headquartered in Little Rock, Ark. Bank of Hawaii (BOH) has consistently been a strong performer and has been among the top 5 institutions since 2006. This is the first time that the bank has taken the top spot in our rankings.

BOH's 2008 performance was driven by its ability to execute a fundamental business model well. In January 2007, the bank implemented a new "2007+" strategic plan that focused on maintaining soundness and discipline in "lending, investing, compliance, capital, and liquidity." BOH shifted from consumer lending to higher-yield commercial lending—all while maintaining a ratio of nonperforming loans to total loans of 0.22%.

This growth was funded by the implementation of innovative strategies to raise core deposits. In the highly competitive market of Hawaii (where the top 4 banks hold 92% of market deposits), BOH not only set aggressive deposit growth goals but changed performance metrics and moved talent around as necessary to enable the achievement of those goals.

In the third and fourth quarters, hitting deposit growth targets became easier for all institutions as consumers pulled their money out of the stock market and put it into banks. To ensure that Hawaiian consumers brought their money to BOH, the bank reworked its entire deposit product offering to better align with customer needs—introducing free checking and simplifying DDA options. The bank also reclassified some deposit balances as interest bearing, creating a product that earned a return for customers on the funds which they had taken out of the markets (but at rates lower than those offered on CDs and, therefore, at a lower cost to BOH).

For other institutions, core banking helped to compensate for declines in revenues from other sources. SVB Financial of Santa Clara, Calif., experienced a near 50% decrease in net income year-over-year due to declining investment fee revenues, dropping from #10 in 2007 to #23 in 2008. The decrease in earnings might have been greater had the bank not been able to both grow loans and replace high-cost borrowings with deposits, thereby improving net interest income, and sustaining a net interest margin that, at 5.42%, was well above the average for both the top 25 (3.88%) and all institutions (3.40%).

Summary statistics

Public banks and thrifts with total assets of $3 billion or more

	Top 25			All Banks		
	2008	2007	% Change	2008	2007	% Change
Average ROAE (%)	13.37	17.08	(3.71)	(4.21)	8.24	(12.46)
Average ROAA (%)	1.20	1.54	(0.33)	(0.35)	0.81	(1.16)
Average Net Interest Margin (%)	3.88	4.05	(0.17)	3.40	3.45	(0.06)
Avg. Noninterest Inc./Tot. Revenue (%)	35.08	32.19	2.89	29.21	28.01	1.20
Average Price/Earnings (x)	19.89	15.15	4.75	24.15	19.73	4.42
Average Capital Ratio (%)	14.29	12.29	2.00	13.76	12.87	0.90
Average Efficiency Ratio (%)	55.68	53.23	2.45	61.62	60.73	0.89
Avg. Nonper. Loans/Total Loans (%)	0.89	0.52	0.37	2.47	1.11	1.36

Source: SNL Financial LC.

Capturing full relationships

SVB Financial also benefited from a highly focused business model. The bank provides banking services only to businesses within specific industry sectors (including technology services, private equity, biotechnology, and premium wine), and to the executives and officers of these businesses and other high net worth individuals. SVB was one of several banks among this year's top performers that made the strategic decision to focus on capturing the full banking relationship of a core group of businesses or consumers. Banks that made this decision and executed it effectively benefited in 2008 as their superior knowledge of target customer segments enabled them to best provide banking services and advice to those customers under adverse conditions.

CVB Financial Corp. of Ontario, Calif. (#10), operates in one of the hardest hit markets in the country—California's Inland Empire. CVB has been able to post strong earnings, despite the large declines in home prices and increases in unemployment, because the bank does not try to serve all segments in its markets. Since its conception, the bank has targeted the "best privately held and/or family owned businesses" with annual revenues of $1 million to $200 million. CVB's loan portfolio is dominated by C&I, CRE, and commercial construction loans. CVB's knowledge of the customers and industries that it serves helped it to maintain a ratio of nonperforming loans to total loans of 0.54%, well below the average ratios of 0.89% and 2.47% for the top 25 and for all institutions, respectively.

Emphasis on cost & efficiency

This year's top performers did not just outperform their peers based on growth in revenues. As in 2007, the top 25 also achieved better-than-average earnings by exhibiting greater expense control. On average, noninterest expenses increased by 9.5% year-over-year for the top performers, compared to 27.0% for all institutions.

For many of the efficiency leaders in 2008's top 25, expense control is a way of life. Westamerica Bancorp., San Raphael, Calif. (#6), for example, has maintained an efficiency ratio of less than 40% for six years running. This strategy is one of the primary reasons that Westamerica has stayed in our top 10 since 2003, despite increased pressures on revenues.

Bank of the Ozarks (#2) has also made the maintenance of efficiency a key part of its overall strategy. For 2008, the bank set the goal of achieving a "sub-40" efficiency ratio and—at 41.74%—it came very close to meeting that goal. Bank of the Ozarks' ratio of noninterest expenses to average assets is just over half that of its peers, at 1.80% compared to averages of 3.16% and 3.26% for the top 25 and for all institutions, respectively. The bank also benefited from decreased market competition, which alleviated pressures on both deposit and loan pricing. This helped the bank to increase its net interest margin by 52 basis points, ending 2008 at 3.96%.

In 2009, banks that can execute well on the basic strategies outlined above—deepening relationships, focusing on target segments, and managing costs effectively—will continue to perform better than peers. Core deposit generation remains critical for success as the cost of other funding sources rises and as deposit products (coupled with payment services) remain central to becoming the customers' primary financial services provider and capturing the full banking relationship. *BJ*