



5 Keys to Improving Your Efficiency Ratio This Year

Agenda

- 1) Efficiency Ratio Defined and In Context
- 2) 5 Keys to Improving Your Efficiency Ratio This Year
- 3) Questions

Efficiency in Context – Efficiency Ratio

$$\text{Efficiency Ratio} = \frac{\text{Non Interest Expense}}{(\text{Net Interest Income} + \text{Non Interest Income})}$$

Bank A drives \$2MM more revenue with \$500,000 less overhead

Examples: Two Texas commercial banks with similar assets (\$300 MM)
At June 30, 2009

Bank A: 1.7% Pre-Tax ROA

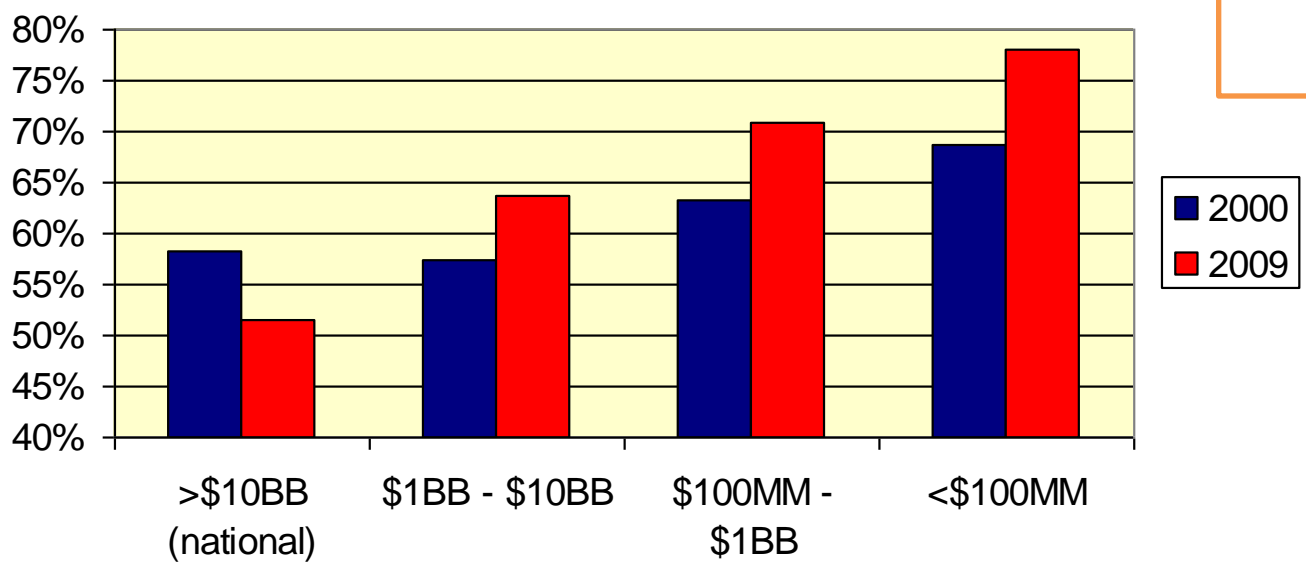
$$\text{Efficiency Ratio} = \frac{\$4,060,000}{(\$6,446,000 + \$1,635,000)} = 50\%$$

Bank B: 1.01% Pre-Tax ROA

$$\text{Efficiency Ratio} = \frac{\$4,557,000}{(\$4,849,000 + \$1,233,000)} = 75\%$$

Efficiency in Context – 10 Year History

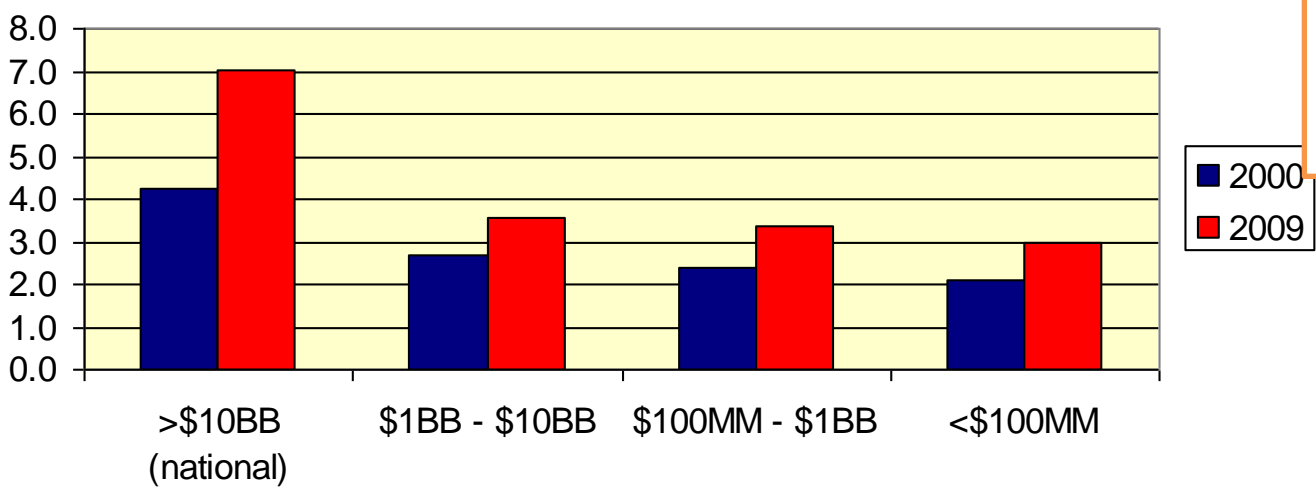
**Efficiency Ratio 10 Year Trend
Texas Commercial Banks**



Texas community banks have become significantly less efficient!

Efficiency in Context – 10 Year History

**Assets per Employee
Texas Commercial Banks
(in \$ millions)**



Texas community banks have become leaner, but it hasn't translated to a better efficiency ratio....Why?

Efficiency in Context – 10 Year History

$$\text{Efficiency Ratio} = \frac{\text{Non Interest Expense}}{(\text{Net Interest Income} + \text{Non Interest Income})}$$

Changes from 2000-2009

	Efficiency Ratio	Non-Interest Expense to Earning Assets	Net Interest Margin	Non-Interest Income to Earning Assets
>\$10BB	Improved by 16%	Worsened by 21%	Worsened by 8%	Worsened by 18%
\$1BB - \$10BB	Worsened by 14%	Worsened by 2%	Worsened by 21%	Improved by 23%
\$100MM - \$1BB	Worsened by 21%	Worsened by 1%	Worsened by 13%	Worsened by 15%
<\$100MM	Worsened by 30%	Worsened by 7%	Worsened by 16%	Worsened by 25%

Efficiency in Context – What Does It Mean

- A poor Efficiency Ratio usually indicates sales, product and overhead problems
- It's one of many metrics to compare and help diagnose; it's not the answer
- Think long-term – efficiency investment today may not pay off for years
- Efficiency Ratio vs Efficient vs Effective
- Teach your people the difference between Productive and Effective

Key #1: Grow the Top Line

- **Improve sales and marketing methods**
 - Move from product-based selling (or “order taking”) to relationship-based advising
 - Nearly everyone should be selling
 - Move beyond branch-centric selling
 - Expand e-marketing
- **Expand share of wallet and retain profitable customers**
- **Grow cash management services to lower cost of funds and/or increase fee income**
- **Diversify fee income**



Most Common Drags on Overhead

People	<p>Ineffective organizational structure (org chart)</p> <p>No personal connection with corporate goals</p> <p>Little accountability</p> <p>Staffing for peak and duplicate functions</p>
Technology	<p>Pay too much</p> <p>Don't maximize existing technology</p>
Facilities	<p>Under-utilized, non-optimized branches</p>
Process	<p>Inefficient manual, and often redundant, processes</p>

Key #2: Optimize FTEs

- Sales accountability for immediate improvement - what's everyone's top daily number for Q4?
- Start move towards right-staffing
 - Fewer, better, higher paid people
 - Goals-based, incentive-based compensation



Key #3: Optimize Technology

- **Technology is likely your most under-utilized asset**
- **Is technology failing to deliver on its promise?**
- **Disconnect is not about the technology, it's how banks buy it and use it**
 - CFIs overspend
 - Buy technology you don't need/don't use
 - Buy more than you need
 - Pay too much when you buy
 - CFIs don't realize benefits (non-optimized)
 - Buy technology that doesn't deliver
 - Buy short-term fixes
 - Pave the cowpath
 - Lack of buy-in = poor utilization
- You need an effective process for evaluating new IT purchases, for negotiating contracts and for managing once you buy

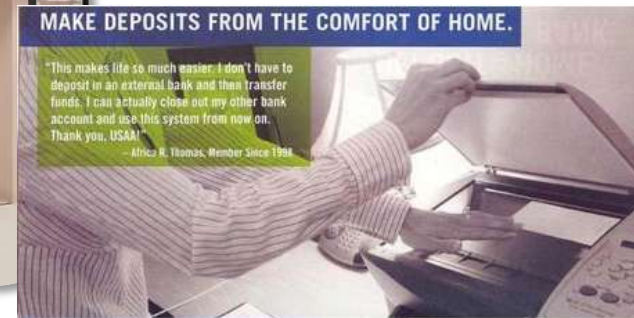


How To Save Money on IT Right Now

- Negotiate contract renewals – accelerate!
- Defer any project without clear ROI or reg requirement
- Accelerate other purchases if appropriate
- Improve use of existing technology
- Purge unused applications, unused services
- Consolidate vendors
- Consider switching from in to out or out to in – any movement will be rewarded
- Unwind custom code
- Milk your Best of Suite strategy just a little longer
- Consolidate servers

Key #4: Optimize Facilities

“Get branches profitable or close them”



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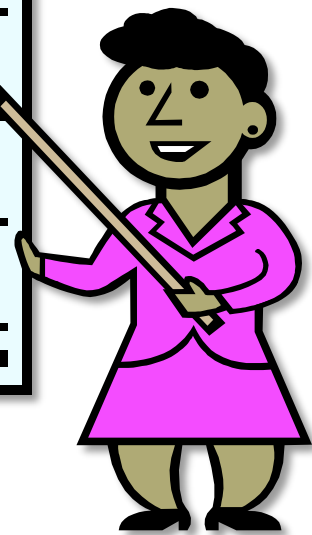
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Branch Profitability Steps for Right Now

- Incent branch president/branch manager and other branch employees for profitability, not just growth
- Migrate from transaction focus to sales focus - get them out of the office!
- Evaluate tiered account management model
- For slow/no growth branches, can you scale back on hours? Cut Saturday hours entirely?
- Do you need several specialists or can you have one generalist with tele- or video- conferencing capabilities to a specialist at the main bank
- Restructure leases, evaluate subleasing

Key #5: Streamline Processes

- **Keys to managing non-interest expense**
 - Optimize FTEs
 - Optimize technology
 - Optimize facilities
- **But process is how they are all tied together!**



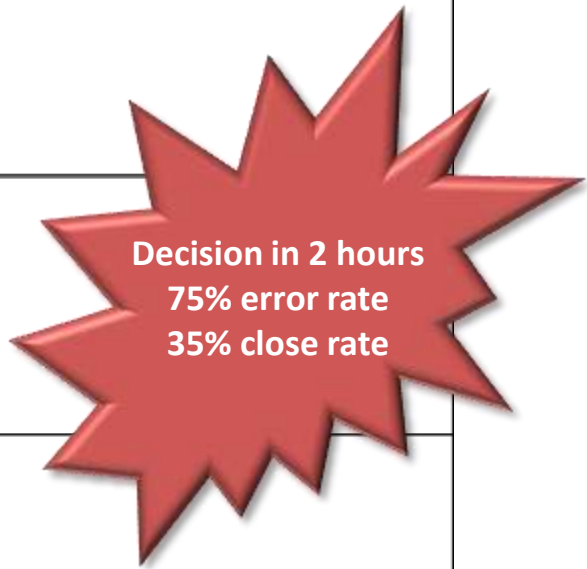
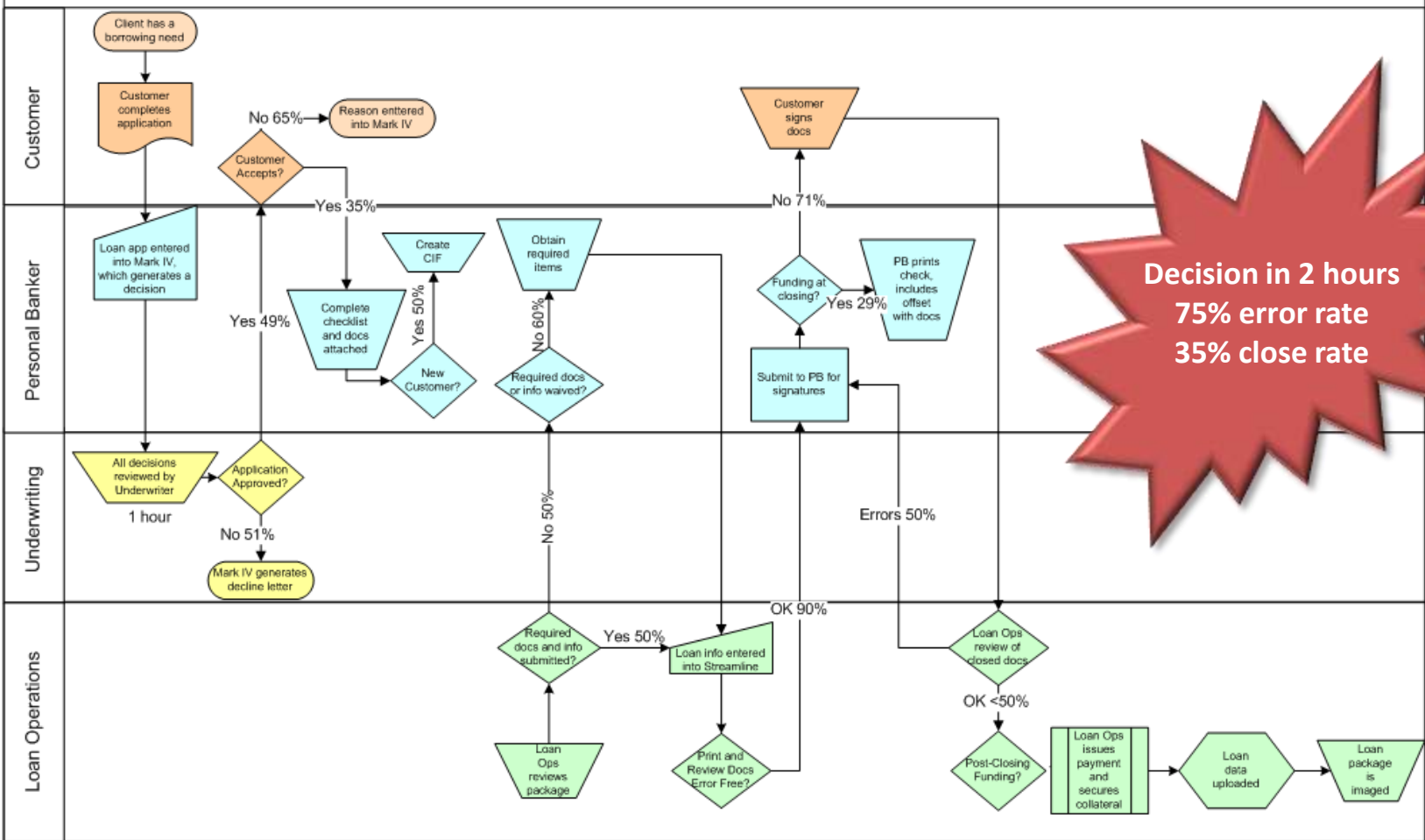
Process Improvement Steps for Right Now

- Pick one important process in your institution
- Map it's current workflow and establish the key metrics (time, quality, cost, risk)
- Set improvement targets for those key metrics
- Design new processes to meet performance targets
- Update policies to support new processes
- Employ effective technology to optimize processes
- Measure and continuously improve

Current Consumer Loan Origination Process Draft

Process: Loan Origination
Sub-Process: Consumer Loan Origination
Department(s): Loan Ops, Underwriting, Branch
Customers: Consumer Loan Customer
Customer Expectation: Quick Decision
Customer Complaints: Takes too long, they went somewhere else, too confusing, dealt w/too many people

Volumes: 400 apps/mo.; 17% close rate (68)
Time: App to Decision (Unsecured-2hrs, RE-24hrs, Car deal 1.5-2hrs); App to Funding (3-5hrs, RE-+3 days=4 total); App to Loaded & Imaged (~3hrs)
Exceptions/Errors: ~75% error rate
Cost (or FTEs/mo.): [Redacted]
Employee Complaints: Too many exceptions, lenders can't see where loan is in process



- Systems Used/Interfaced:**
- Mark IV
 - Streamline
 - Jack Henry SilverLake

- Inputs:**
- Application and customer-submitted docs
 - Checklist

- Outputs:**
- Decline letter
 - Loan docs
 - Funding
 - Loan booked on SilverLake

- Policies:**
- [Redacted]

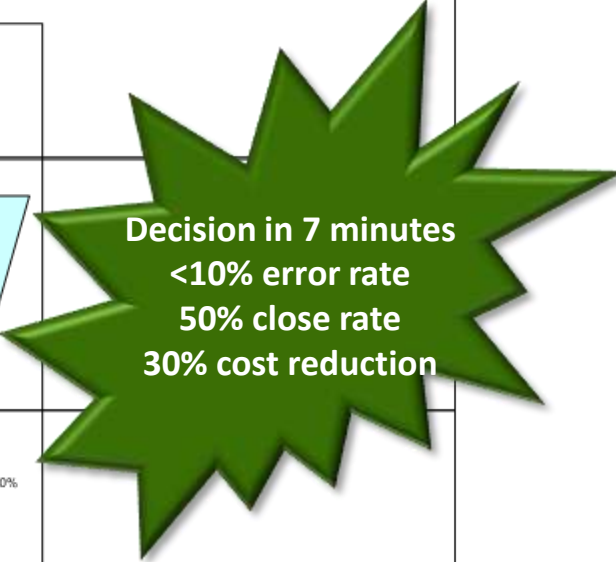
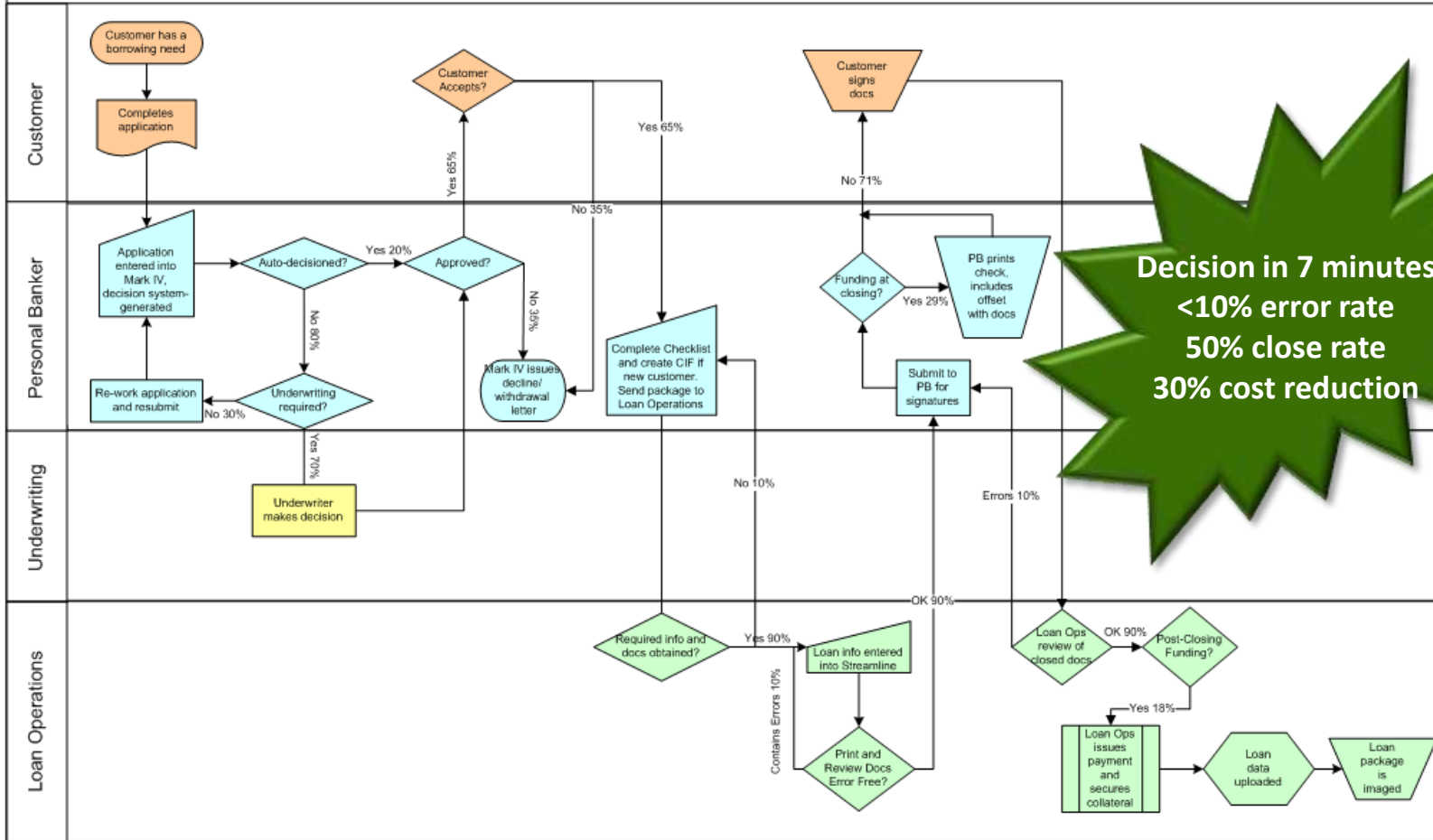
- Improvement Opportunities:**
- How do we get to a decision in 7 minutes
 - Score-based instead of rules-based?
 - PB's understanding Mark IV

Proposed Consumer Loan Origination Process

Process: Loan Origination
Sub-Process: Consumer Loan Origination
Department(s): Loan Ops, Underwriting, Branch
Customers: Consumer Loan Customer
Customer Expectation: Quick Decision
Customer Complaints: Takes too long, they went somewhere else, too confusing, dealt w/too many people

Volumes: 400 apps/mo.; 42.25% close rate
Time: 1. Unsecured and auto loan with no underwriting required: < 7 minutes 44% of the time, 30 minutes app to closing 2. Unsecured and auto loan with underwriting required < 30 minutes 56% of the time, 60 minutes app to closing 3. RE 1 hour decision, 3 days to close (due to regulatory requirements)

Exceptions/Errors: [Redacted]
Cost (or FTEs/mo.): [Redacted]
Employee Complaints: Too many exceptions, lenders can't see where loan is in process



Systems Used/Interfaced:

- Mark IV
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- Jack Henry SilverLake

Inputs:

- Application and customer-submitted docs
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Outputs:

- Decline letter
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Policies:

- [Redacted]

Improvement Opportunities:

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- Score-based instead of rules-based?
- PB's understanding Mark IV

Other Streamlining Tactics

- Integrate systems
- Eliminate paper
- Maximize image, explore least cost routing
- Workflow tools



Ready for the Hard Questions



Questions



How We Might Be of Help

For more information on how Abound might help your institution with

- Improving efficiency and redesigning processes
- Negotiating core, EFT, Internet banking, etc. contracts
- Evaluating your use of technology and/or creating technology plans
- Developing payments and retail delivery strategies
- Developing commercial cash management strategies
- Improving loan origination and servicing processes
- Upgrading consumer or commercial Internet banking systems
- Pre-acquisition due diligence, early termination penalty negotiations and post-merger integration

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