Branching Out

Independent Banks Have Two Choices:
Grow Or Get Gobbled Up By Holding Companies

In the span of less than a week, the landscape of independent banking in South Louisiana shifted dramatically.

On March 29, ISB Financial Corp., the holding company for Iberia Savings Bank, announced it was acquiring a major thrift institution in metropolitan New Orleans and would increase in size by over 40 percent as the result of the move. Just four days later, the owners of the largest independent bank in Louisiana — the Calcasieu Marine National Bank — confirmed what many in Lake Charles had already suspected. They had decided to sell the $774 million bank to Hibernia Corp. of New Orleans.

These two announcements symbolized the strategies which independent banks in the region must pursue in the years ahead. Consolidation of the banking industry is taking place at a rapid pace. Those financial institutions not affiliated with one of the large holding companies must either expand their banks in a major way or be prepared to sell out to a larger institution with the resources to stimulate such growth.

"The idea is to make your franchise as valuable as possible by increasing market share," says Peter Gwaltney, vice president and chief operations officer for the Louisiana Bankers Association. "Eat or be eaten. It's the law of survival in nature, and it's increasingly the environment in the financial industry.

In the past several months, two independent banks in the Acadiana area decided that their shareholders were better off by merging with a larger bank. In September, the board of directors of First National Bank in St. Mary Parish agreed to sell their institution to Whitney Bank of New Orleans, and the board of New Iberia Bancorp, parent of New Iberia Bank, announced in January that it would enter into negotiations with Whitney. The proposed sale of the New Iberia institution comes after a bitter internal battle between stockholders who wanted to maintain the bank's independence and those who wanted to liquidate its positions.

The high-priced announcement of the First National/Whitney deal touched off a healthy run-up in the stock prices of other independent banks in the area as market players speculated that more acquisitions were on the way. Observers suggested that it was only a matter of time before the big holding companies gobbled up all of the mid-sized and small banks operating in the area, as they have done in other parts of the country.

But the officers of independent banks insist that there is still a place for their institutions in the era of consolidation. A loosening of federal regulations, increased access to technology and innovative ways to satisfy shareholders' demands for liquidity allow the mid-sized banks to compete against the behemoths and do so profitably.

"I don't care what anybody says — there won't be only three banks left in Louisiana," MidSouth National Bank president Rusty Cloutier told The Times last year.

SB Financial Corp. positioned itself for serious growth when it became a stockholder-owned institution with shares traded in the national over-the-counter market. The company went public in early 1995 and raised a massive amount of capital which allowed it to acquire other financial entities.

It made a small move in that direction in late 1995 by announcing its purchase of the Bank of Lafayette. But that was a minor step compared to the decision to buy Jefferson Bancorp, a $265.9 million savings and loan which operated seven full-service offices in Jefferson and Orleans parishes.

"The merger of these two highly profitable, strongly capitalized companies is an important strategic move for ISB Financial and reflects the company's commitment to expand throughout South Louisiana," president Larry Mouton said in a release announcing the acquisition. Later he told The Advocate, "Competition is driving these consolidations ... you have to grow to survive."

The move was clearly aimed at allowing ISB to remain in control of its destiny. "I think they want to keep their independence, that's a smart way to go," says John Moore, who follows regional banking for the Memphis-based brokerage house Morgan, Keegan & Co. With so much capital on its balance sheet from last year's stock offering, the company was a ripe acquisition target.

Bank analyst Woody Briggs of Chaffe & Associates in New Orleans had noted as much last year when he suggested that ISB needed strong asset growth to deal with its capital position. "He [Mouton] needs to have a billion in good assets, at a minimum," Briggs told The Times. "He needs to find a way to get that bank bigger or give some of that capital back to investors."

He's on track to hit the goal Briggs has suggested. When the mergers with Jefferson and Bank of Lafayette are completed, ISB should have assets in the $900 million range.

But growth alone won't satisfy shareholders. ISB must also maintain its profitability by expanding services and increasing loans. To that end, the bank recently hired longtime Lafayette banker Ronnie Foret as executive vice president. His mission will be to expand the bank's commercial lending operation; commercial loans are typically one of the most profitable markets for a bank.

ISB's acquisition of Jefferson Bancorp was the most dramatic growth move

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undertaken by a local independent bank in the last year. But other players in the market have also been taking steps to increase their market share. MidSouth National Bank has been pursuing a strategy of expansion to the southeast. The Lafayette-based institution opened a branch in New Iberia and acquired a small bank in Jeanerette. It plans to open an office in Morgan City shortly.

Lafayette has provided expansion opportunities for numerous banks in the Acadiana area. St. Martin Bank & Trust of St. Martinville, St. Landry Bank & Trust, American Bank of Opelousas, Gulf Coast Bank of Abbeville, New Iberia Bank and Rayne State Bank have all opened branches in Lafayette in recent years. In many cases, these banks made their move in response to soft loan demand in their hometowns. "The way to improve profitability is to grow. Sometimes in a community you've grown all you can," says one bank official.

Richard Seale, president of First Bank, N.A., formerly First National Bank, in Crowley, faced that dilemma. Crowley is a mature market which generates healthy deposits, says the veteran banker. But where to lend that money? Seale decided to look to the west. "You have so many banks represented in Lafayette. We felt that Lake Charles was a better opportunity," he says.

The company opened a branch in the economically thriving city and hired a Lake Charles native who had worked for Calcasieu Marine to run it. With the sale of Calcasieu Marine, First Bank finds itself in a market with no locally-owned commercial banks. "Our niche will be those customers looking for an independent bank with localized service," says Seale.

But bankers like Seale still face daunting tasks in maintaining their independence, given today's increasingly complex financial environment. In particular, customers are demanding that their banks provide more convenient service by allowing them to pay bills over the phone and use debit cards instead of checks. More sophisticated customers want to conduct financial transactions over their home computers using online services. The demand for that service will likely explode in the coming years.

Can a relatively small institution like First Bank of Crowley, with assets of just over $90 million, afford to buy, install and maintain computer systems of this magnitude? Seale says the solution is for independent banks to pool their resources. "We are going to have to find a way to band together and buy technology," he says.

Gwaltney of the Louisiana Bankers Association says smaller banks are already starting to figure out how to compete in the high-tech arena. "We've seen a lot of smaller country banks finding telephone banking to be affordable," he says. And he notes that an independent bank based in the tiny community of Delhi in northeastern Louisiana has a home page on the World Wide Web. "They are out in the middle of a cotton field," he says.

While technology is creating new challenges for independent bankers, they are getting relief in another area which had led many to consider selling out in the past. Several years ago, the owners of some small banks were prepared to throw in the towel because of an increasing burden of government oversight.

In response to the banking crisis of the 1980s, the federal government began to tighten the regulatory screws on banks in order to detect problems before they became disasters. Small banks found themselves inundated with paperwork and had to increase personnel to comply with the government's mandates. That drove up costs.

The load has lightened in recent years. Congress has exempted smaller banks from some of the more burdensome rules, say bankers.

"The bureaucrats may be off the banker's back. But in some cases, that spot is now being occupied by shareholders.

Increased acquisition activity has increased the value of most bank stock. When owners of that stock see the premium prices that are being paid for other banks, they often become eager to unload their own shares at a healthy profit. But management typically wants to remain independent rather than sell out to an out-of-town institution which will have its own ideas on how to run the bank. The result: conflict between top executives and their shareholders.

Such a scenario unfolded at the New Iberia Bank throughout 1994 and 1995 and caused serious division within the family that was the dominant owner of the institution. Similar tensions exist at other
banks, though none have been played out so publicly.

Local independent bankers say they are taking steps to ensure that such conflicts do not erode their institutions. Several local banks have listed their shares on one of the national exchanges so that a stockholder who wants to unload his holdings can do so more easily.

“The idea is to make your franchise as valuable as possible by increasing market share.”

— Peter Gavaltry

But that option can be costly and time-consuming. In lieu of that, banks maintain a list of individuals who want to buy and sell stock in the institution. They attempt to match the parties together and thus create more liquidity in the stock.

Paul Dignan, executive vice president and chief operating officer of St. Martin Bank and Trust, says his bank tries to maintain shareholder ownership by increasing

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GREENSPAN: TECHNOLOGY RE-ShAPING BANKING INDUSTRY

Bankers, are you getting tired of the rat race? Alan Greenspan has this advice: Rats, start your engines.

The chairman of the Federal Reserve Board doesn’t say something so colloquially, as Louisiana’s bankers found in a recent forum where Greenspan spoke about the future of their business. And the national press focused on Greenspan’s cautious remarks (his trademark); the economy’s going along pretty well, he says — which were taken to suggest no sudden easing of interest rates is in sight.

What didn’t get as much attention, perhaps because it’s kind of depressing if you’re one of today’s rat-racing bankers, is that Alan Greenspan, Futurist, had to say about the medium-term long-term prospects of the financial services business.

Banking is being driven by the same underlying forces which are reshaping the general economy. “Relentless technological change” should raise productivity and standards of living in the next century — but at the cost, Greenspan says, of “a marked degree of uncertainty in the work force.”

“Human skills are subject to obsolescence at a rate perhaps unprecedented in our history,” Greenspan says, leading to a “focus on downsized companies with more sophisticated technological labor inputs.”

What that means to the banker is the impact of direct communication with customers, custom-tailored products, computerization of financial markets and deregulation that will erode distinctions between roles like stockbroker, banker or insurance agent. “The evolution of financial technology alone has changed forever our ability to place financial institutions into neat and clear categories,” Greenspan says.

He uses the example of the spread of interstate banking in the last decade to illustrate his point that “market forces make it impossible to maintain old systems.” Additionally, the large-scale market in derivatives did not exist until technology of sufficient sophistication to crunch those kinds of numbers came into general use.

All these changes, however, does not mean there won’t be a demand for traditional services from households and small businesses, in particular. “Banks of all types will continue to deliver banking services of all kinds,” he says. “Well-managed smaller banks can and will exist alongside larger banks.”

Greenspan suggests that smaller banks that are closer to their customers can succeed because they are in a position to know their customers’ business and creditworthiness. He called this “a franchise large institutions cannot match.”

Greenspan made these remarks at a forum in New Orleans sponsored by U.S. Rep. Richard Baker, R-Baton Rouge, a member of the House Banking Committee. On the platform with Baker and Greenspan was Banking Committee chair- man Jim Leach, who also emphasizes that smaller banks must invest in technology to be competitive. Leach, an Iowa Republican, says that the small bank is vulnerable to banks like Citicorp or insurance giants if they fail to provide the same number of options for customers.

“Small banks that are on top of technology are going to be winners in the years ahead,” he says. “Small banks that lag behind in technology are going to have a very hard time.”

— LANNY KELLER

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activity in Louisiana lags behind other states. The banking market is still not as consolidated as in many other Southern states.

"It's really amazing to me the number of banks in Louisiana that are between $250 million and $1 billion," says Morgan Keegan's Moore. "Strung out along Highway 90 between New Orleans and Lafayette, there are a number of fairly small banks."

Despite the recent upsurge, merger activity in Louisiana lags behind other states. The banking market is still not as consolidated as in many other Southern states.

"It's really amazing to me the number of banks in Louisiana that are between $250 million and $1 billion," says Morgan Keegan's Moore. "Strung out along Highway 90 between New Orleans and Lafayette, there are a number of fairly small banks."

One institution which has caught Moore's eye is Teche Federal Savings Bank, based in Franklin. Teche, like ISB, converted to a stock charter last year and is sitting on a treasure trove of capital. But the institution, with about $322 million in assets, has not moved into the acquisition mode since raising the money through the sale of stock.

Moore says Teche has more capital than it needs. "The regulators like you. I don't know if it's all that good for shareholders," he says.

The outcome, he speculates, is that Teche could be a seller rather than a buyer. "They are often cited as the next big takeover candidate," he says.

Patrick Little, president of Teche, disputes that notion. "We didn't convert to be acquired. We converted to get the benefits of stock ownership," says Little. He says the bank is expanding its services and increasing the number of deposit accounts, primarily through its no-fees checking.

Not surprisingly, Little won't comment on possible acquisition opportunities. However, he pronounces himself satisfied with Teche's progress since its conversion last year. "We're on target to do the things we want to do," he says.

The protestsations of independent bankers notwithstanding, banks will be sold in the years ahead. That's without question. And that offers opportunities for investors who want to take advantage of increasing values of local bank stocks.

One method is to buy shares in banks which are traded on the major national exchanges. MidSouth and Teche's stock can be bought through the American Stock Exchange, while ISB is traded over-the-counter. Investors who owned these stocks last year enjoyed a nice increase in the value of their holdings.

"That can take a while," the bank and waiting for some returns. "The stock very seldom trades. Usually, the only time it trades is through death and inheritance. But if you're willing to hold it, it can be a good investment," says Henry Mayer Jr., senior vice president at Morgan Keegan & Co's Lafayette office.

Mayer, a former national bank examiner, matches up buyers and sellers of stock in three local banks, which he declined to identify. The stock in these banks is thinly traded and not listed on a national exchange.

Mayer believes that the stock of such banks is a good investment, though he warns that it is not right for everyone. Dividends are often low or non-existent, and the investor may have a hard time finding a buyer for his stock if he decides to unload it. Nevertheless, Mayer thinks these shares have upside potential. "I think anybody who can get local banks' stocks, it's a wonderful investment. Eventually, they are going to get gobbled up," he says. "The price of most of the local banks' stocks has gone up substantially. I wish I'd bought some myself."