

To curb efficiency ratios, community banks continue cost-cutting

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With the first round of 2016 earnings releases behind them, community banks continue to manage their efficiency ratios with cost-saving efforts.

S&P Global Market Intelligence looked at results for the quarter ended March 31 among banks with less than \$10 billion in assets. The analysis includes banks that reported

earnings as of May 6. The smallest banks in the analysis, those with less than \$1 billion in assets, reported the highest efficiency ratio on a median basis — 73.13%. Banks with between \$1 billion and \$5 billion in assets reported a median efficiency ratio of 64.75%. Among the largest community banks — those between \$5 billion and \$10 billion in assets — the median efficiency ratio was 59.89%. All three groups saw median efficiency ratios decline year over year.

Sandler O'Neill & Partners analyst Stephen Scouten noted that low rates have limited the power of the “revenue side of the equation,” leaving banks searching for cost saves in areas like branch rationalization. Regulatory expenses are also a factor on the expense side, Scouten said, particularly for the banks over \$6 billion that have a higher chance of moving past the \$10 billion benchmark after a deal.

Community bank earnings recap: less than \$1B in assets

Earnings reported up to May 6

Rank	Company name (ticker)	City, state	Total assets Q1'16 (\$B)	Efficiency ratio		YOY operating revenue growth (%)	ROAA	
				Q1'16 (%)	YOY change (pps)		(%)	YOY trend*
Lowest efficiency ratio								
1	Parke Bancorp Inc. (PKBK)	Sewell, NJ	0.93	47.28	6.56	4.70	1.32	▲
2	County Bancorp Inc. (ICBK)	Manitowoc, WI	0.91	50.41	0.20	11.90	0.97	▼
3	California First National Bancorp (CFNB) ¹	Irvine, CA	0.86	50.43	-0.29	-0.38	0.76	▼
4	Greene County Bancorp Inc. (MHC) (GCBC) ¹	Catskill, NY	0.85	56.08	-2.84	11.68	1.05	▲
5	Norwood Financial Corp. (NWFL)	Honesdale, PA	0.76	56.96	4.11	-1.33	1.00	▼
6	Summit State Bank (SSBI)	Santa Rosa, CA	0.52	57.68	21.75	9.86	1.02	▼
7	Marlin Business Services Corp. (MRLN)	Mount Laurel, NJ	0.80	58.39	5.51	2.98	1.88	▼
8	Auburn National Bancorp. Inc. (AUBN)	Auburn, AL	0.83	59.67	-2.61	-0.52	1.07	▲
9	First Bank (FRBA)	Hamilton, NJ	0.92	60.16	-5.46	10.30	0.60	▼
10	American River Bankshares (AMRB)	Rancho Cordova, CA	0.63	61.24	-10.04	8.71	0.86	▲
Highest efficiency ratio								
1	Peoples Financial Corp. (PFBX)	Biloxi, MS	0.70	96.94	4.65	-8.48	0.05	▲
2	Anchor Bancorp (ANCB) ¹	Lacey, WA	0.42	96.83	5.13	9.31	0.10	▼
3	Sunshine Bancorp Inc. (SBCP)	Plant City, FL	0.52	95.55	-29.79	134.51	0.12	▲
4	Georgetown Bancorp Inc. (GTWN)	Georgetown, MA	0.31	92.85	9.00	5.63	0.11	▼
5	Old Point Financial Corp. (OPOF)	Hampton, VA	0.86	91.73	10.69	-0.87	0.47	▼
6	United Security Bancshares Inc. (USBI)	Thomasville, AL	0.58	90.84	3.32	-0.92	0.22	▼
7	Broadway Financial Corp. (BYFC)	Los Angeles, CA	0.39	89.58	5.52	NA	0.64	▼
8	Hamilton Bancorp Inc. (HBK) ²	Towson, MD	0.39	89.22	-18.12	31.07	0.12	▲
9	HopFed Bancorp Inc. (HFBC)	Hopkinsville, KY	0.89	88.71	10.25	-7.73	0.23	▼
10	Bay Bancorp Inc. (BYBK)	Columbia, MD	0.46	88.41	5.55	-12.93	0.16	▼
Bank and thrift median[^]				73.13	-0.39	6.63	0.71	▲

Data compiled May 9, 2016.

Analysis limited to top/bottom 10 banks and thrifts traded on the Nasdaq, NYSE or NYSE MKT by efficiency ratio for the quarter ended March 31, 2016. Only companies with total assets below \$1 billion as of March 31, 2016, that reported earnings up to May 6 are shown.

All data shown is for the quarter ended March 31, 2016, and is based on GAAP filings.

¹ The quarter ended March 31, 2016, is the fiscal third quarter of 2016 for the company.

² The quarter ended March 31, 2016, is the fiscal fourth quarter of 2016 for the company.

* The year-over-year comparison represents the change in actual values, not the change in values rounded to two decimal places.

[^] Median for all major exchange-traded banks and thrifts with assets below \$1 billion that have reported earnings up to May 6.

Year-over-year compares the quarter ended March 31, 2016, to the quarter ended March 31, 2015.

ROAA = return on average assets; YOY = year-over-year; pps = percentage points; NA = not available

Source: SNL Financial, an offering of S&P Global Market Intelligence

Small banks, too, feel the pinch from regulation. "One of the harder things to deal with being a smaller institution is all of the regulatory costs," said John Marzullo, CFO at Hamilton Bancorp Inc. The \$393 million Maryland bank reported an efficiency ratio of 89.22% for the quarter, down more than 18 percentage points year over year but still on the high end of the spectrum.

"We have to be in line with some of the stuff that larger banks are doing. We're obviously not as efficient because of our scale, to accommodate some of those expenses," Marzullo said. Like Scouten, he highlighted the challenges low rates present. "Net interest margin is getting tighter. I think a lot of banks are looking to noninterest income to supplement that and more innovative ways to generate noninterest income compared to just the interest side of things," he said.

Marzullo noted that Hamilton Bancorp is continually looking for ways to cut costs, including evaluating its ven-

dor contracts and shopping around for less costly options. "We're a publicly traded institution," he said. "[The efficiency ratio] is a key metric that our investors are looking at and I think in this rate environment and this economy, it is something that banks are heavily focused on."

with long-held strategies of cost-cutting managed down their efficiency ratios despite the challenging environment. Conway, Ark.-based Home BancShares Inc. reported a 37.54% efficiency ratio for the first quarter, down 3.30 percentage points year over year. During the bank's earnings call, executives touted their ongoing efforts to push the ratio lower. Donna Townsell, senior executive vice president of corporate efficiencies, pointed out that the bank is keeping a "watchful eye on expenses" as revenue inches upwards. She noted that the bank closed four branches in the first quarter and a fifth in the current quarter.

"We have said it before, it was hard to get here and it is equally hard to stay here," Townsell said.

Community bank earnings recap: \$1B to \$5B in assets

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Rank	Company name (ticker)	City, state	Total assets Q1'16 (\$B)	Efficiency ratio		YOY operating revenue growth (%)	ROAA	
				Q1'16 (%)	YOY change (pps)		(%)	YOY trend*
Lowest efficiency ratio								
1	Hingham Institution for Savings (HIFS)	Hingham, MA	1.85	33.98	-3.67	11.76	1.19	▲
2	Oritani Financial Corp. (ORIT) ¹	Township of Washington, NJ	3.60	39.26	-0.92	1.70	1.27	▼
3	ConnectOne Bancorp Inc. (CNOB)	Englewood Cliffs, NJ	4.09	42.25	1.26	10.84	1.03	▼
4	Preferred Bank (PFBC)	Los Angeles, CA	2.68	43.35	1.47	23.60	1.20	▼
5	Lakeland Financial Corp. (LKFN)	Warsaw, IN	3.81	47.86	-1.97	7.01	1.29	▼
6	Green Bancorp Inc. (GNBC)	Houston, TX	3.85	47.92	-11.23	69.83	0.20	▼
7	West Bancorp. Inc. (WTBA)	West Des Moines, IA	1.76	48.19	-0.06	4.55	1.31	▲
8	Stonegate Bank (SGBK)	Pompano Beach, FL	2.45	50.01	-6.51	7.09	1.12	▲
9	Republic Bancorp Inc. (RBCAA)	Louisville, KY	4.25	50.64	-8.56	22.98	1.60	▲
10	First of Long Island Corp. (FLIC)	Glen Head, NY	3.23	51.18	-0.64	13.63	0.94	▼
Highest efficiency ratio								
1	The Bancorp Inc. (TBBK)	Wilmington, DE	4.38	108.01	22.05	0.02	-0.99	▼
2	Bank of Commerce Holdings (BOCH)	Redding, CA	1.08	104.69	33.77	1.68	-0.37	▼
3	Sun Bancorp Inc. (SNBC)	Mount Laurel, NJ	2.17	93.62	-20.20	-7.32	0.15	▼
4	Pacific Mercantile Bancorp (PMBC)	Costa Mesa, CA	1.10	91.20	-8.61	4.72	0.11	▲
5	AmeriServ Financial Inc. (ASRV)	Johnstown, PA	1.12	87.31	3.95	-4.37	-0.45	▼
6	Provident Financial Holdings Inc. (PROV) ¹	Riverside, CA	1.17	87.20	9.76	-15.20	0.51	▼
7	Capital City Bank Group Inc. (CCBG)	Tallahassee, FL	2.79	85.69	-2.38	1.70	0.24	▲
8	Republic First Bancorp Inc. (FRBK)	Philadelphia, PA	1.48	84.52	-6.17	24.04	0.30	▲
9	Fidelity Southern Corp. (LION)	Atlanta, GA	4.10	83.89	14.84	-2.13	0.46	▼
10	Orrstown Financial Services Inc. (ORRF)	Shippensburg, PA	1.29	82.59	-1.18	6.16	0.80	▼
Bank and thrift median[^]				64.75	-1.12	7.05	0.88	▲

Data compiled May 9, 2016.

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Scouten of Sandler O'Neill said Home BancShares has focused on managing expenses for years. "They've shown a propensity to manage expenses over the long haul," he said. "It's not a new phenomenon for them."

Birmingham, Ala.-based ServisFirst Bancshares Inc. is another bank on the low end of the efficiency ratio scale. Sandler O'Neill analyst Brad Milsaps attributed the low figure to the fact that ServisFirst does not have a large network of branch or retail locations. Instead, the business-focused bank spreads its commercial lenders around each of its markets for a more efficient strategy, Milsaps said.

Banks like Seattle-based HomeStreet Inc. on the high end of the efficiency ratio spectrum are hopeful that they can improve through the end of the year. HomeStreet

reported an efficiency ratio of 84.27% in the first quarter, up 7.44 percentage points year over year. During the company's earnings call, management said the bank expects its core efficiency ratio to fall to the mid to low 60% range by the end of 2016. On the expense side, executives said that "overhang" from the bank's latest deal, five new office openings and the lack of material loan sales or securities gains impacted the ratio for the first quarter.

More broadly, Scouten said that the efficiency ratio is an "exclusionary" metric for many investors who tend to raise concerns only when the figure is abnormally high or low. "Some of these banks have taken a long time to work past the last cycle and haven't really gotten the cost out of their banks," he added.

Community bank earnings recap: \$5B to \$10B in assets

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				Q1'16 (%)	YOY change (pps)		(%)	YOY trend*
Lowest efficiency ratio								
1	BofI Holding Inc. (BOFI) ²	San Diego, CA	7.71	31.66	-2.40	55.50	1.95	▲
2	Home BancShares Inc. (HOMB)	Conway, AR	9.40	37.54	-3.30	28.14	1.78	▲
3	ServisFirst Bancshares Inc. (SFBS)	Birmingham, AL	5.38	39.33	-1.04	19.62	1.35	▲
4	Eagle Bancorp Inc. (EGBN)	Bethesda, MD	6.13	41.17	-4.39	13.06	1.54	▲
5	Capitol Federal Financial Inc. (CFFN) ¹	Topeka, KS	9.32	42.47	-1.45	NA	0.77	▲
6	Great Western Bancorp Inc. (GWB) ¹	Sioux Falls, SD	9.94	44.95	-6.79	8.85	1.24	▲
7	Opus Bank (OPB)	Irvine, CA	6.93	45.11	-7.77	33.11	1.02	▲
8	CVB Financial Corp. (CVBF)	Ontario, CA	7.92	46.08	3.31	3.34	1.21	▲
9	FCB Financial Holdings Inc. (FCB)	Weston, FL	7.84	46.37	-2.60	21.28	1.19	▲
10	BBCN Bancorp Inc. (BBCN)	Los Angeles, CA	8.07	48.06	-2.68	6.27	1.20	▲
Highest efficiency ratio								
1	HomeStreet Inc. (HMST)	Seattle, WA	5.42	84.27	7.44	12.95	0.51	▼
2	Banc of California Inc. (BANC)	Irvine, CA	9.62	83.17	7.31	24.90	0.89	▲
3	Boston Private Financial Holdings Inc. (BPFH)	Boston, MA	7.41	72.55	3.78	0.34	1.03	▼
4	OFG Bancorp (OFG)	San Juan, PR	6.87	70.11	19.74	-18.59	0.81	▲
5	Banner Corp. (BANR)	Walla Walla, WA	9.75	67.81	2.35	82.71	0.73	▼
6	Northwest Bancshares Inc. (NWBI)	Warren, PA	8.92	67.31	0.74	15.36	0.81	▼
7	Heartland Financial USA Inc. (HTLF)	Dubuque, IA	8.25	67.20	-2.48	23.08	1.00	▲
8	Flushing Financial Corp. (FFIC)	Uniondale, NY	5.81	65.52	1.14	9.57	0.66	▼
9	Central Pacific Financial Corp. (CPF)	Honolulu, HI	5.24	65.01	-4.56	3.56	0.87	▲
10	Park National Corp. (PRK)	Newark, OH	7.43	64.28	2.64	5.34	1.01	▼
Bank and thrift median[^]				59.89	-1.35	10.89	1.01	▲

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