

Increasing Loan Portfolio Profitability in a Slow Growth Environment

A Live Webinar Presented by Austin Associates, LLC

Presenters:

Jeffrey Morris

Managing Director & Principal
Austin Associates



Michael Scheopner

Executive Vice President, Chief Risk Manager
Landmark National Bank



Austin Associates' – Practice Areas

- **Investment Banking**
- **Strategic Consulting**
- **Financial Management**
- **Insurance and Financial Services**
- **Technology Solutions**
- **Risk Management and Compliance**

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Financial Management – Practice Areas

- **Asset Liability Management – Reporting & Consulting**
 - **Net Interest Margin Simulations**
 - **Earnings at Risk – Economic Value of Equity**
 - **Third Party Review of In-House ALM Models**

- **Commercial Loan Pricing – Internet Based Software**
- **Customer, Product & Branch – Profitability Reporting**

- **Operational Efficiency Improvement Recommendations**
- **Branch Network Rationalization Studies**
- **Management Dashboards**

Landmark National Bank

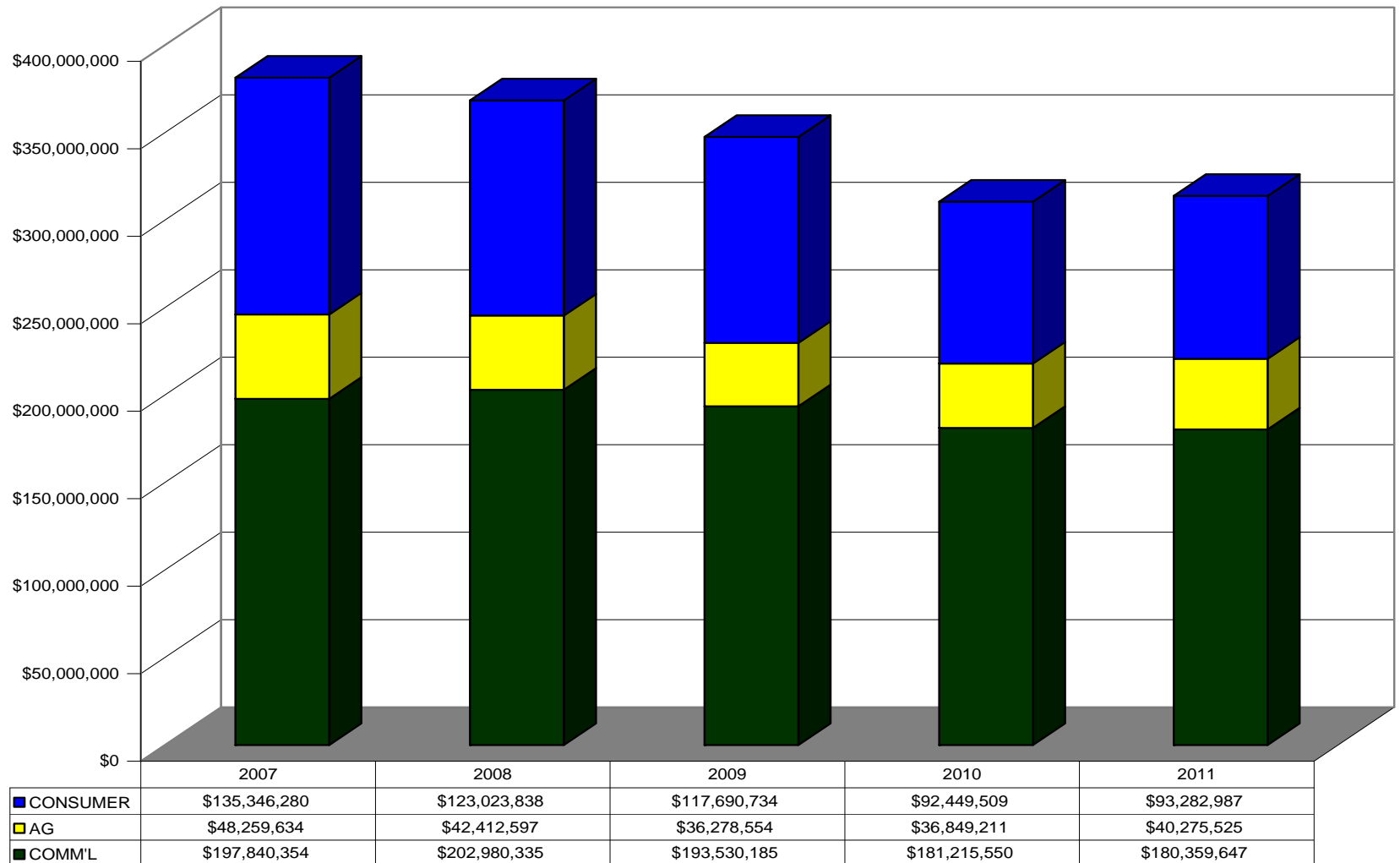
- **Headquartered in Manhattan, Kansas**
- **Serves 7 MSA's with 22 Branches in 17 Cities**
- **Population of 2.9 Million**
- **\$620 M in Assets**
 - **L/D Ratio = 71%**
- **Capital / Assets = 12.64%**
 - **Risk Based Capital = 15.73%**

Landmark National Bank

- **\$310 M in Loans**
 - **\$220 M in Comm'l. & Ag. Loans**
- **Well Diversified by Industry and Geography**
 - **1- 4 Family from across entire state**
 - **Commercial Volume from Central Region**
 - **Agri-Business from Western Region**

Declining Loan Balances

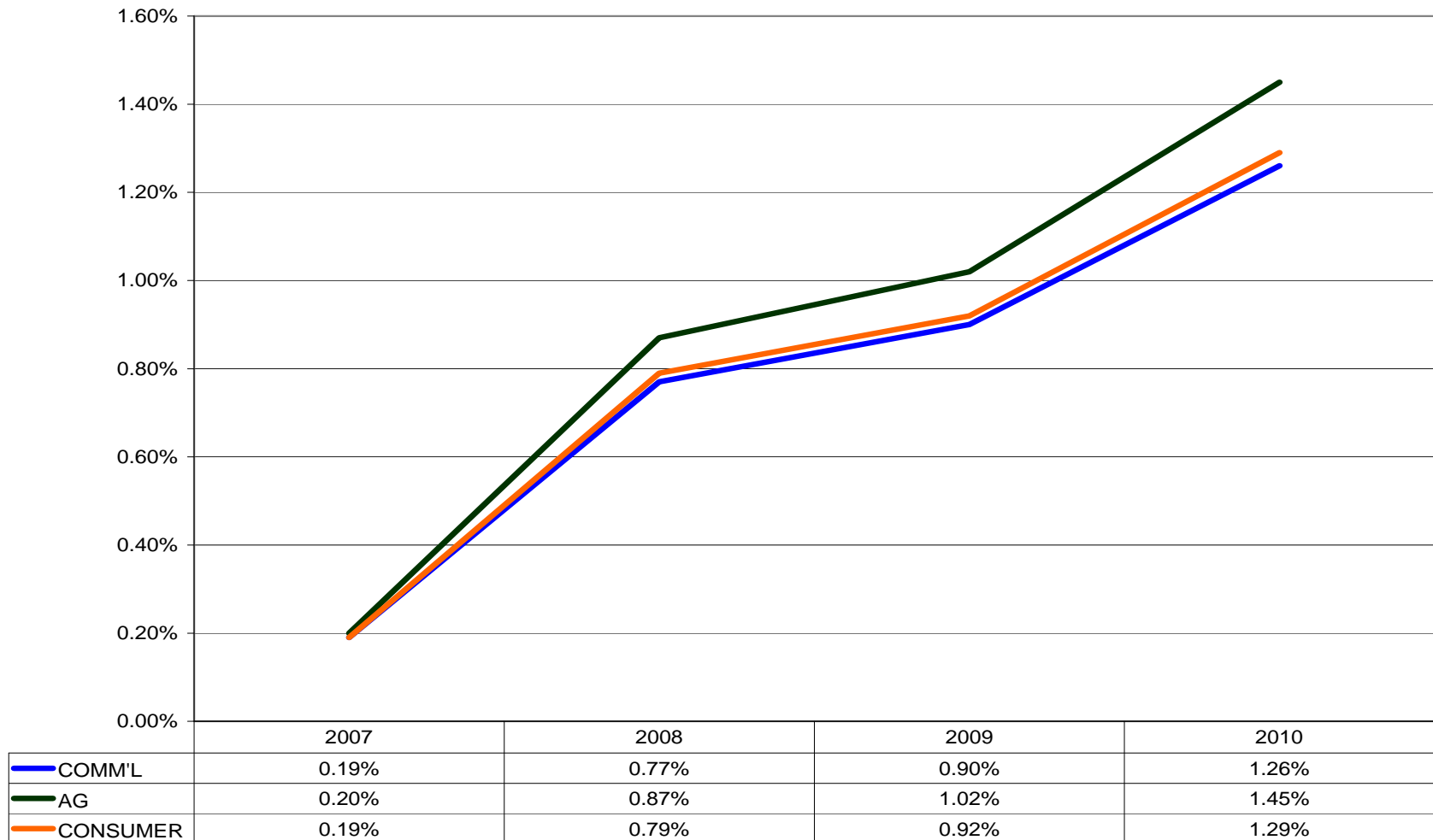
Landmark National Bank



Source: Austin Profitability System

Loan Losses by Product Type – Up until 2010

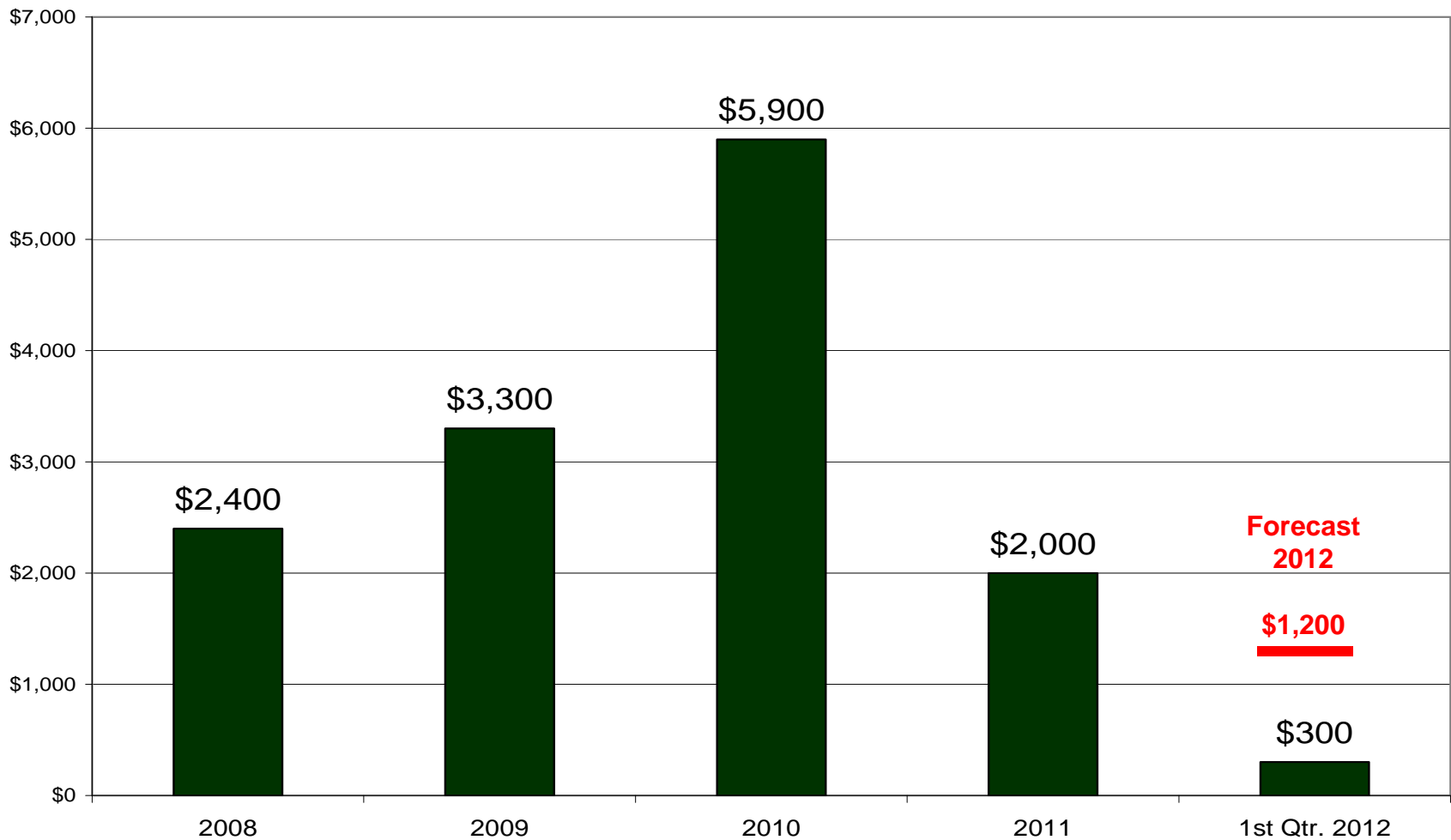
Landmark National Bank



Source: Austin Profitability System

PFLL Trends

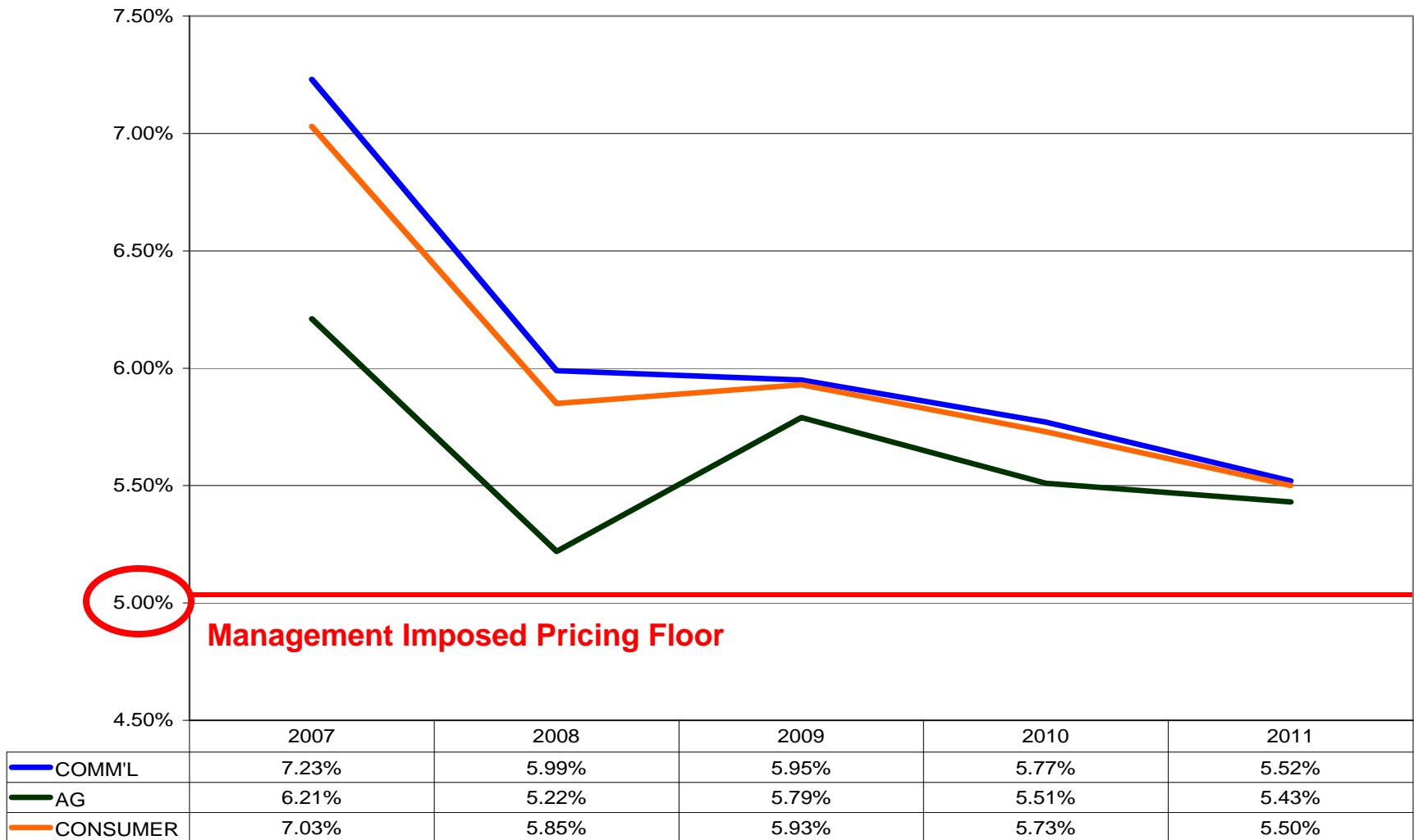
Landmark National Bank



Source: SNL Financial
Based on weighted average data

Declining Loan Yields

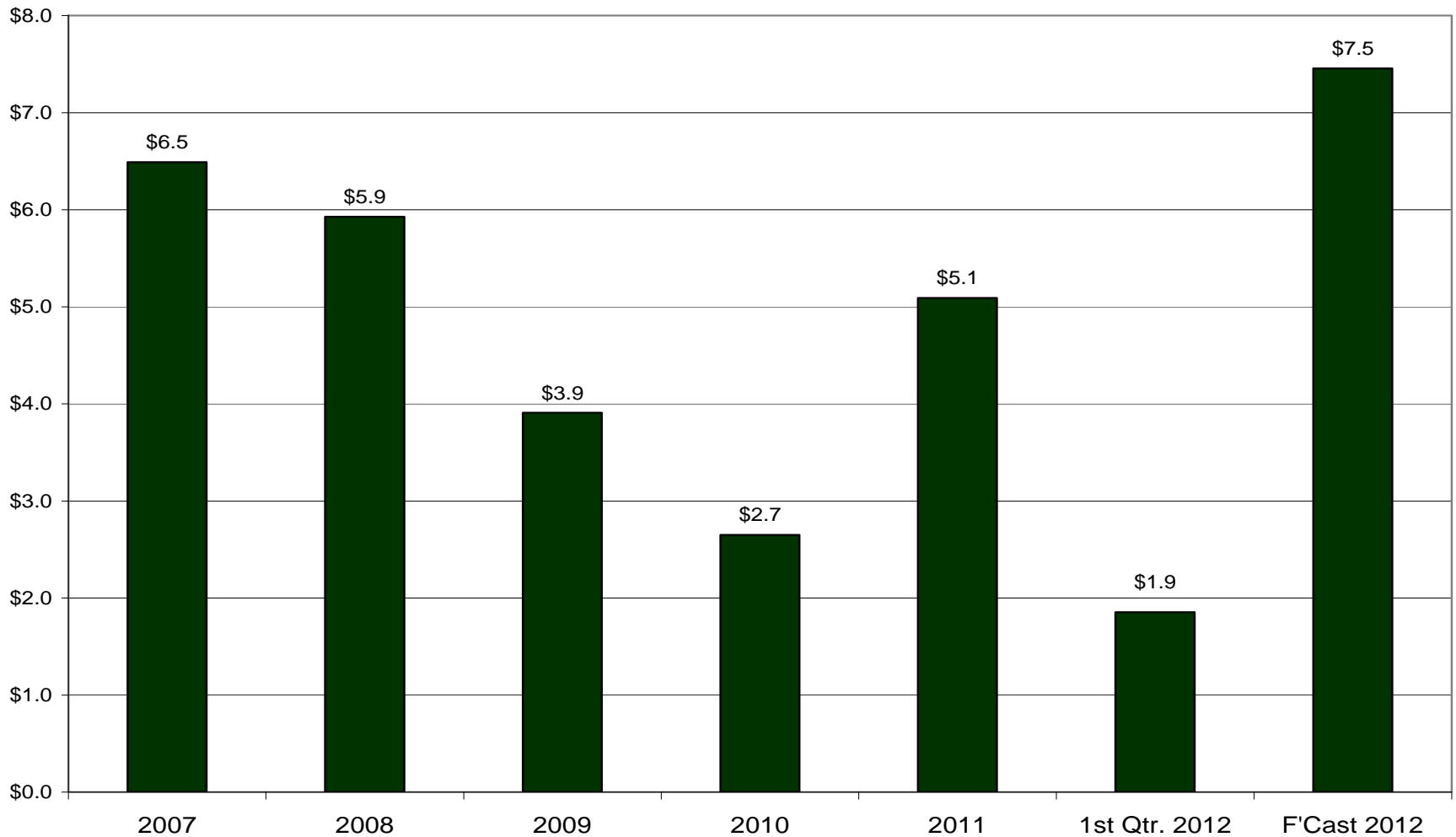
Landmark National Bank



Source: Austin Profitability System

Net Income Trends

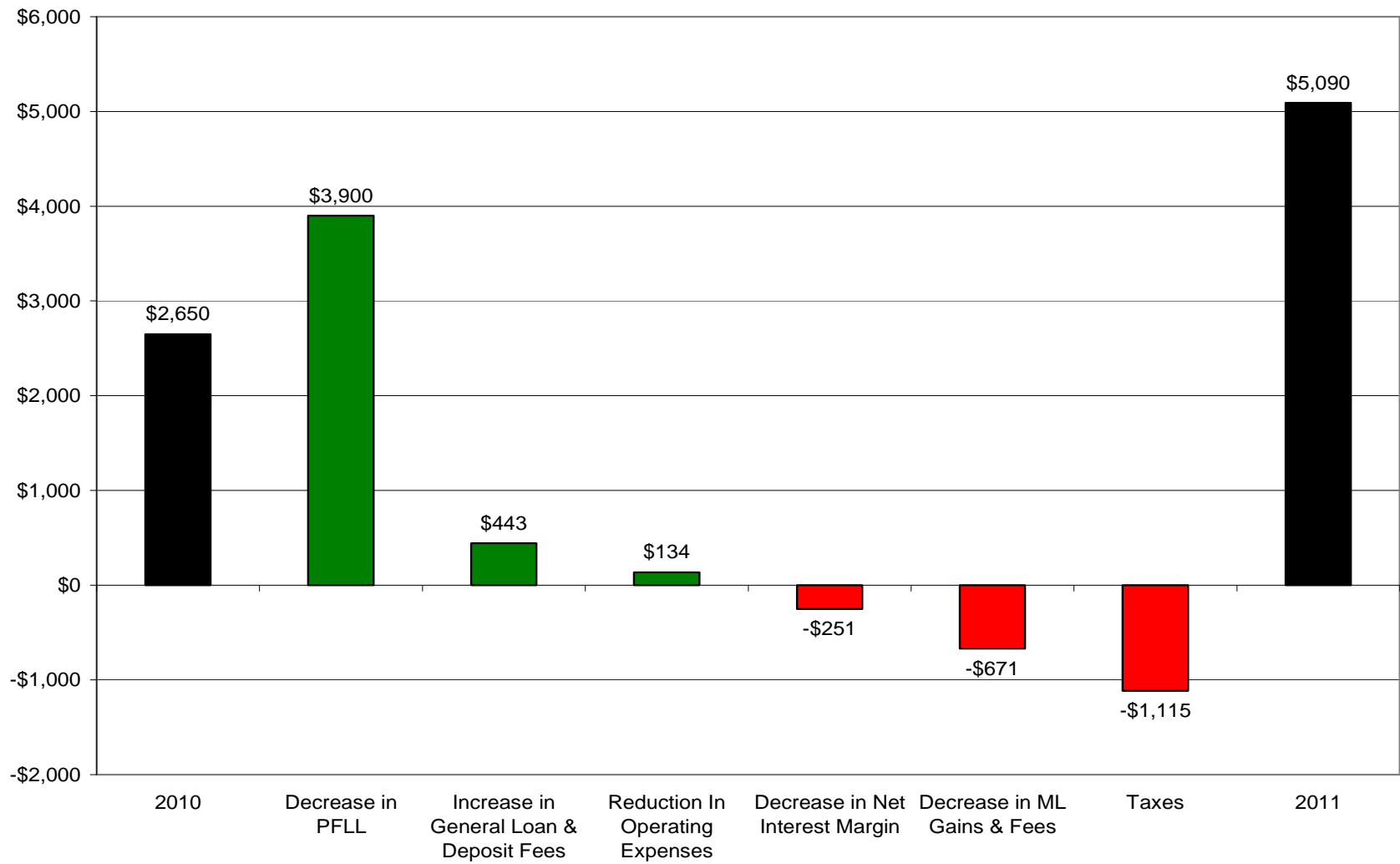
Landmark National Bank



Source: SNL Financial
Based on weighted average data

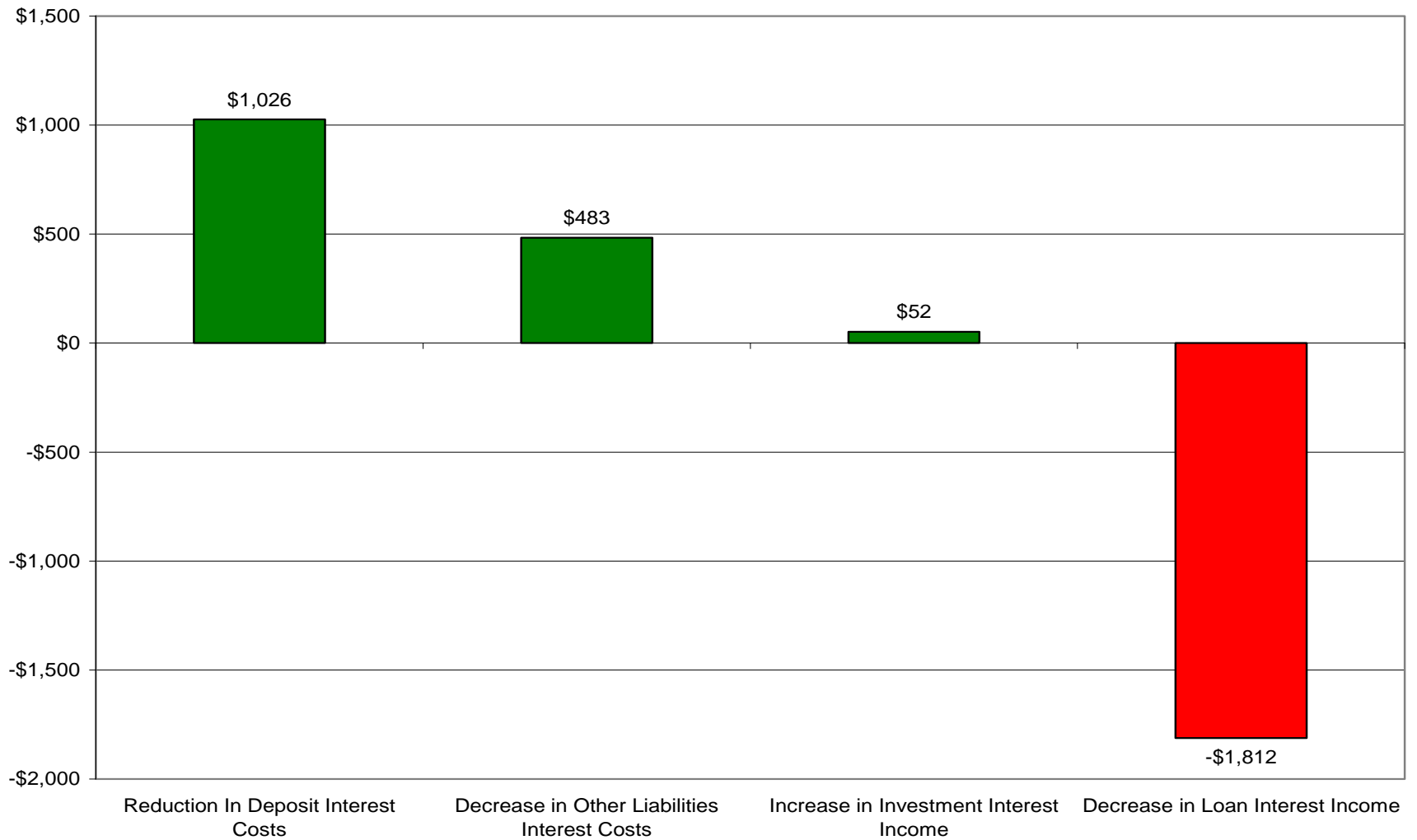
Profit Changes – 2010 vs 2011

Landmark National Bank



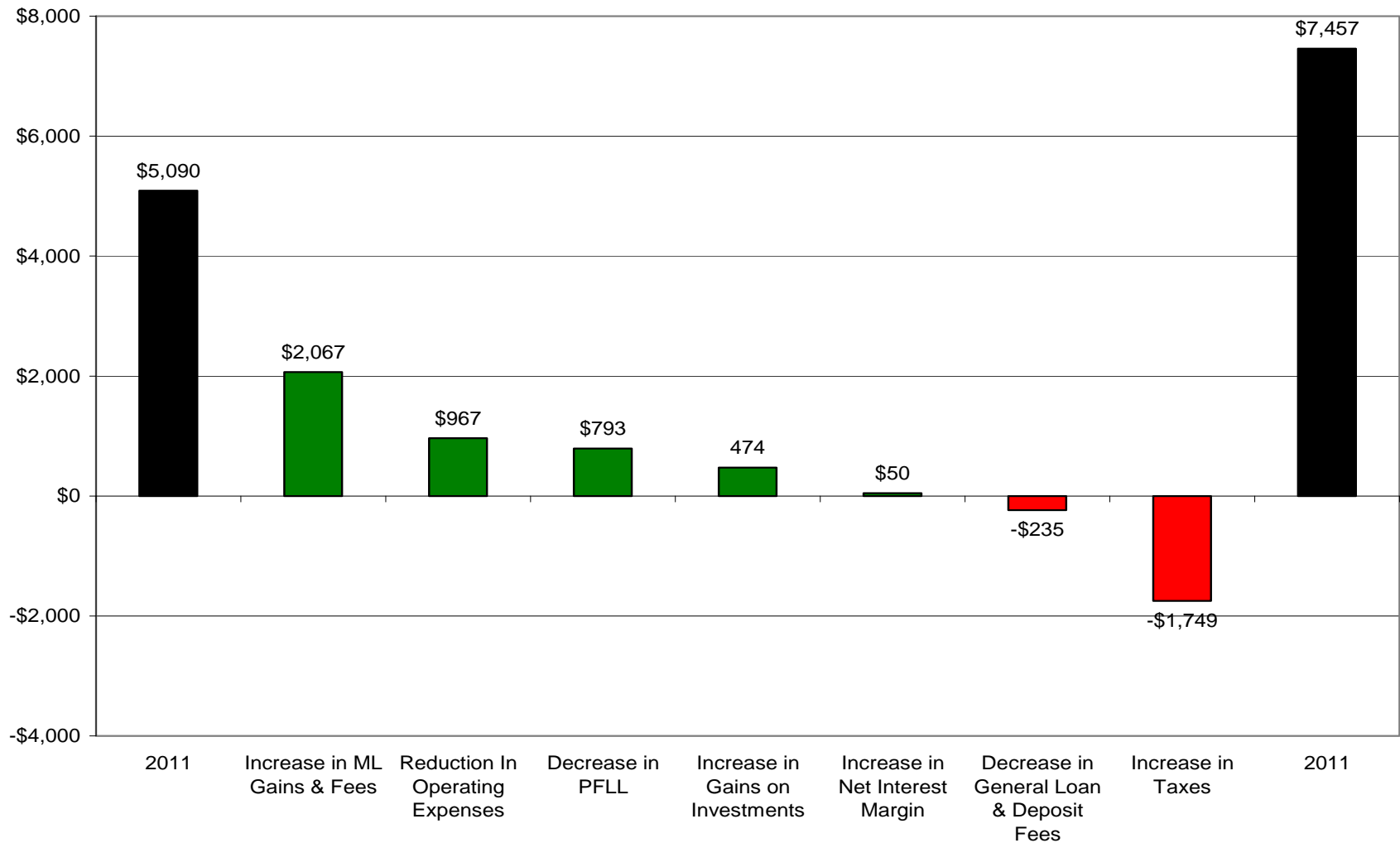
Net Interest Margin Changes – 2010 vs 2011

Landmark National Bank



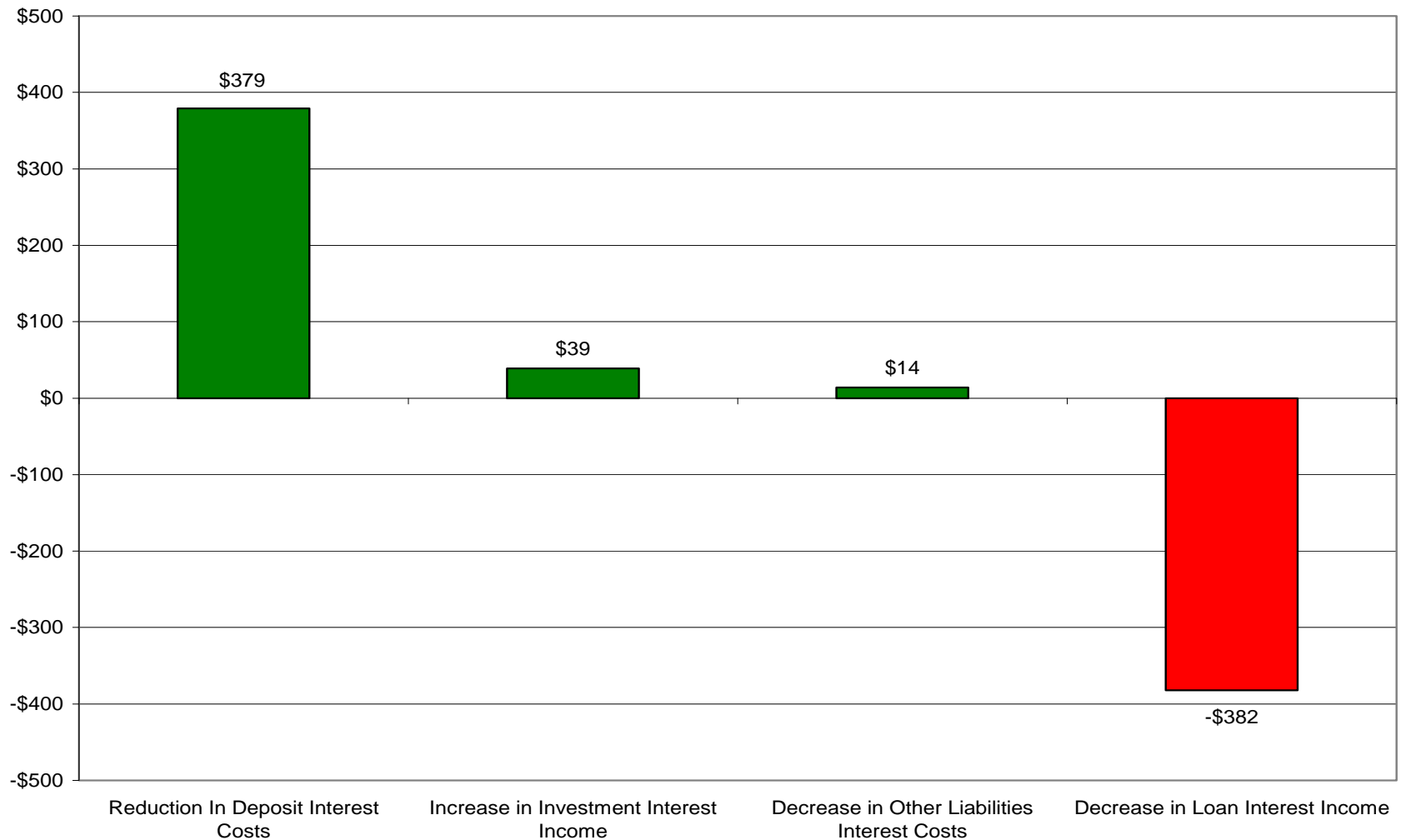
Profit Changes – 2011 vs 2012 Forecast

Landmark National Bank



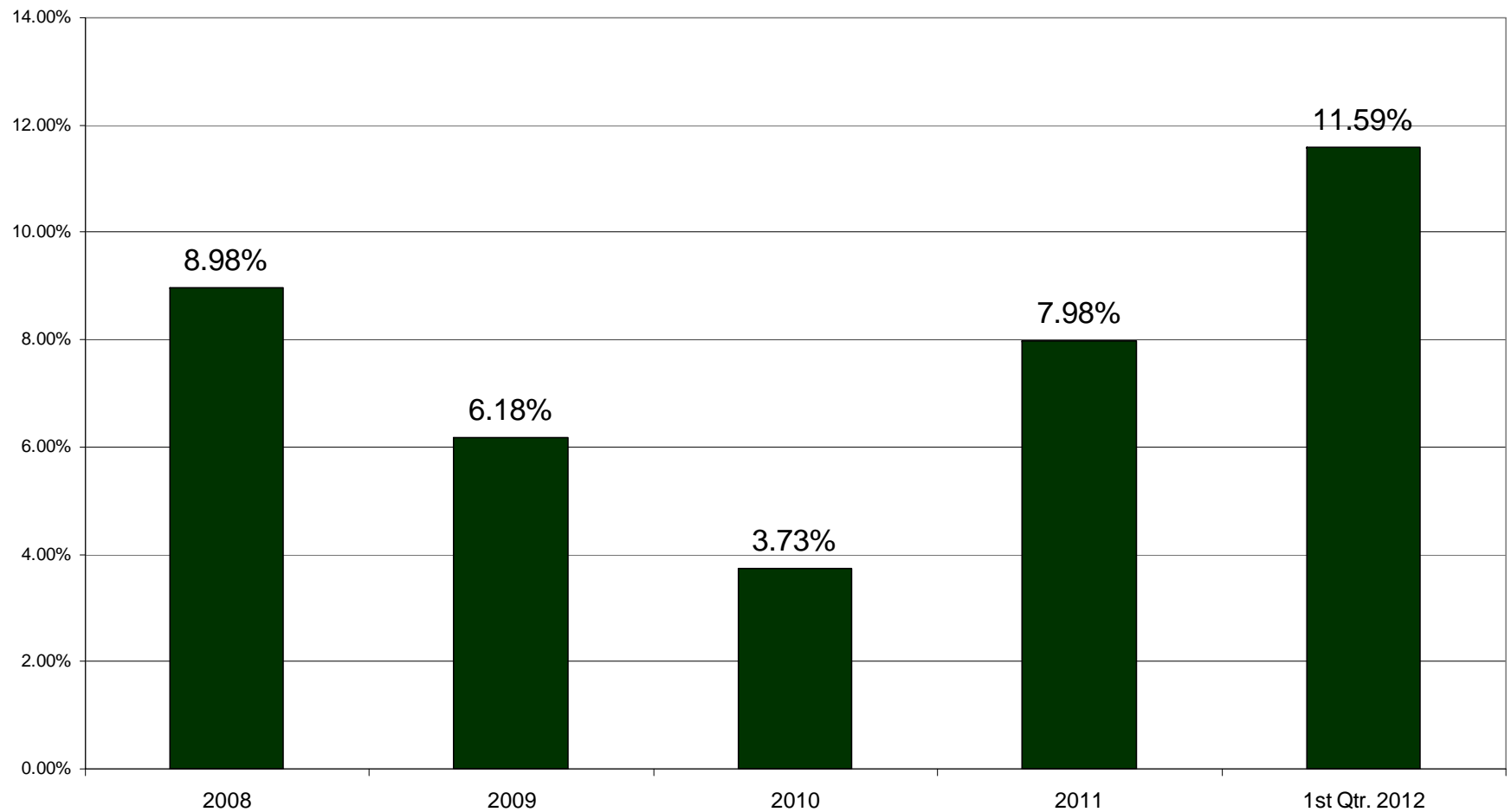
Net Interest Margin Changes – 2011 vs 2012

Landmark National Bank



ROE Trends

Landmark National Bank



Source: SNL Financial
Based on weighted average data

Loan Pricing Discipline – Process Over Time

Landmark National Bank

Began with Organizational Decision to Improve Process

Due Diligence on Models Available – (Internal & Marketplace Solutions)

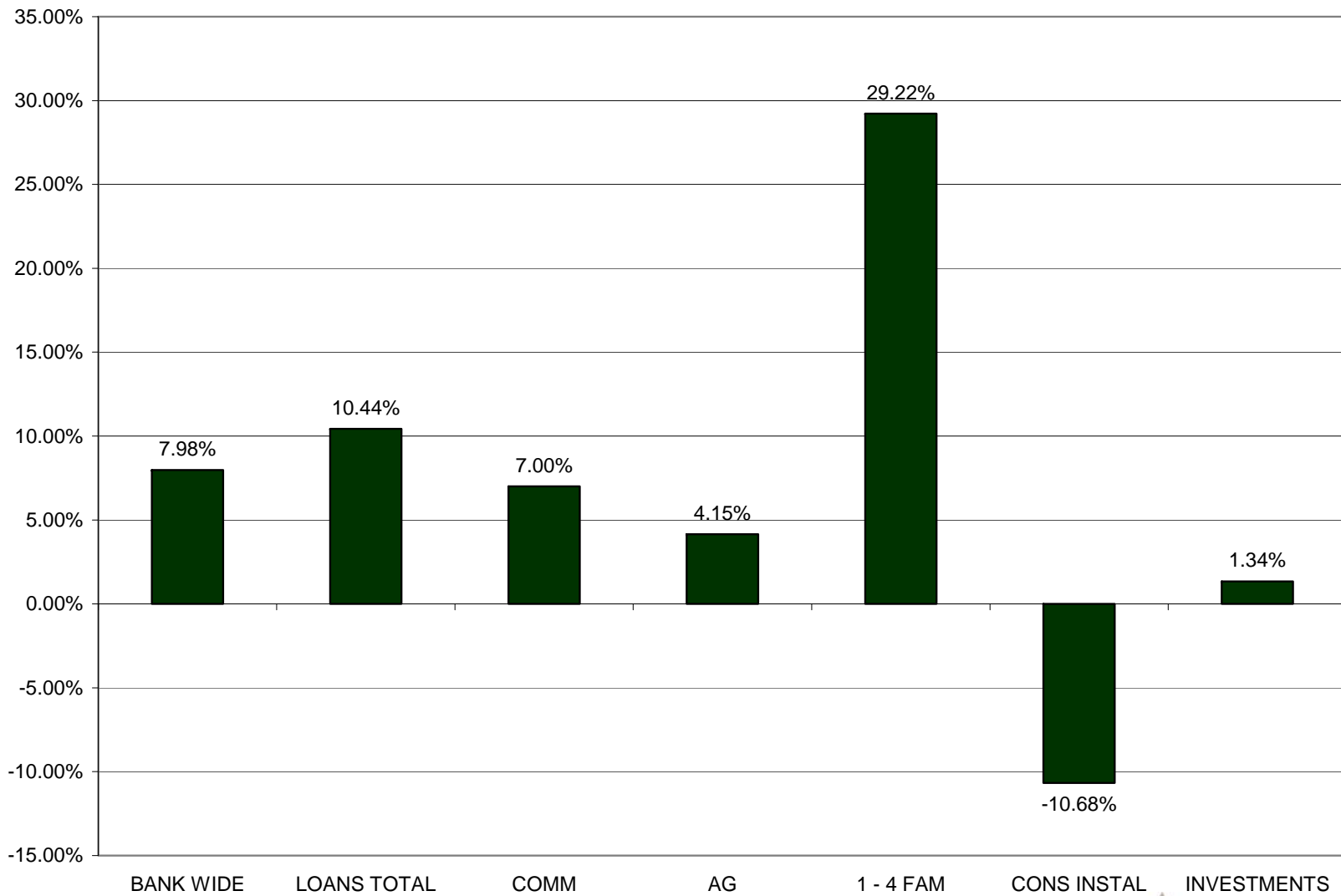
Selected Austin Associates Commercial Loan Pricing System

- Internet Based Solution, w/ Interface to Core, Tier II Profitability Analysis, Providing ROE reporting by Customer & Officer
- Customization / Calibration / Training
- Initial Implementation – “Recommended” Use of Model
- Phase 2 – Mandatory for all Loans > \$ “X” – ROE > ,= Matrix Target
- Ongoing Tracking of ROE by Officer by Senior Management

ROE by Product Type

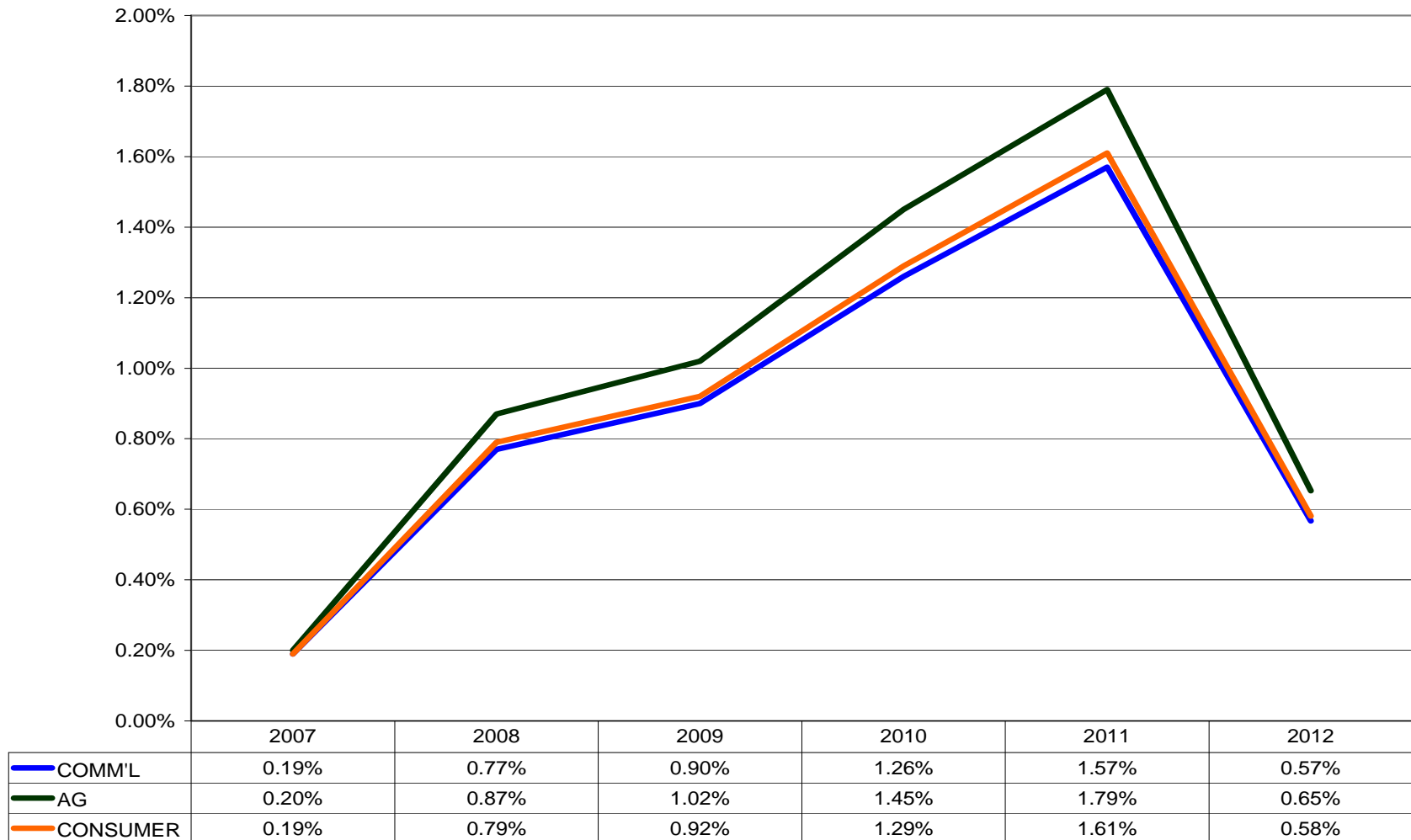
Landmark National Bank

Full Year - 2011



Loan Losses by Product Type – Up to Current

Landmark National Bank



Source: Austin Profitability System

ROE Actuals – Commercial & Ag Relationships

Landmark National Bank

Current Actual Portfolio Returns – By Loan Size – By Product

<u>Product Type</u>	<u>< \$250 K</u>	<u>\$250 - \$500 K</u>	<u>\$500 K - \$ 1 M</u>
Commercial RE	5.28%	9.99%	13.86%
C & I Lending	2.42%	12.32%	13.07%
Agricultural	6.56%	9.84%	12.89%

ROE Targets – Commercial & Ag Relationships

Landmark National Bank

Target / Goal Portfolio Returns – By Loan Size – By Product

<u>Product Type</u>	<u>< \$250 K</u>	<u>\$250 - \$500 K</u>	<u>\$500 K - \$ 1 M</u>
Commercial RE	8.00%	12.00%	15.00%
C & I Lending	6.00%	14.00%	16.00%
Agricultural	10.00%	12.00%	15.00%

(Note: Each of the above targets is based on what management believes is an appropriate level of profitability IMPROVEMENT for each loan type / relationship size.)

ROE Trends – Tracking by Officer

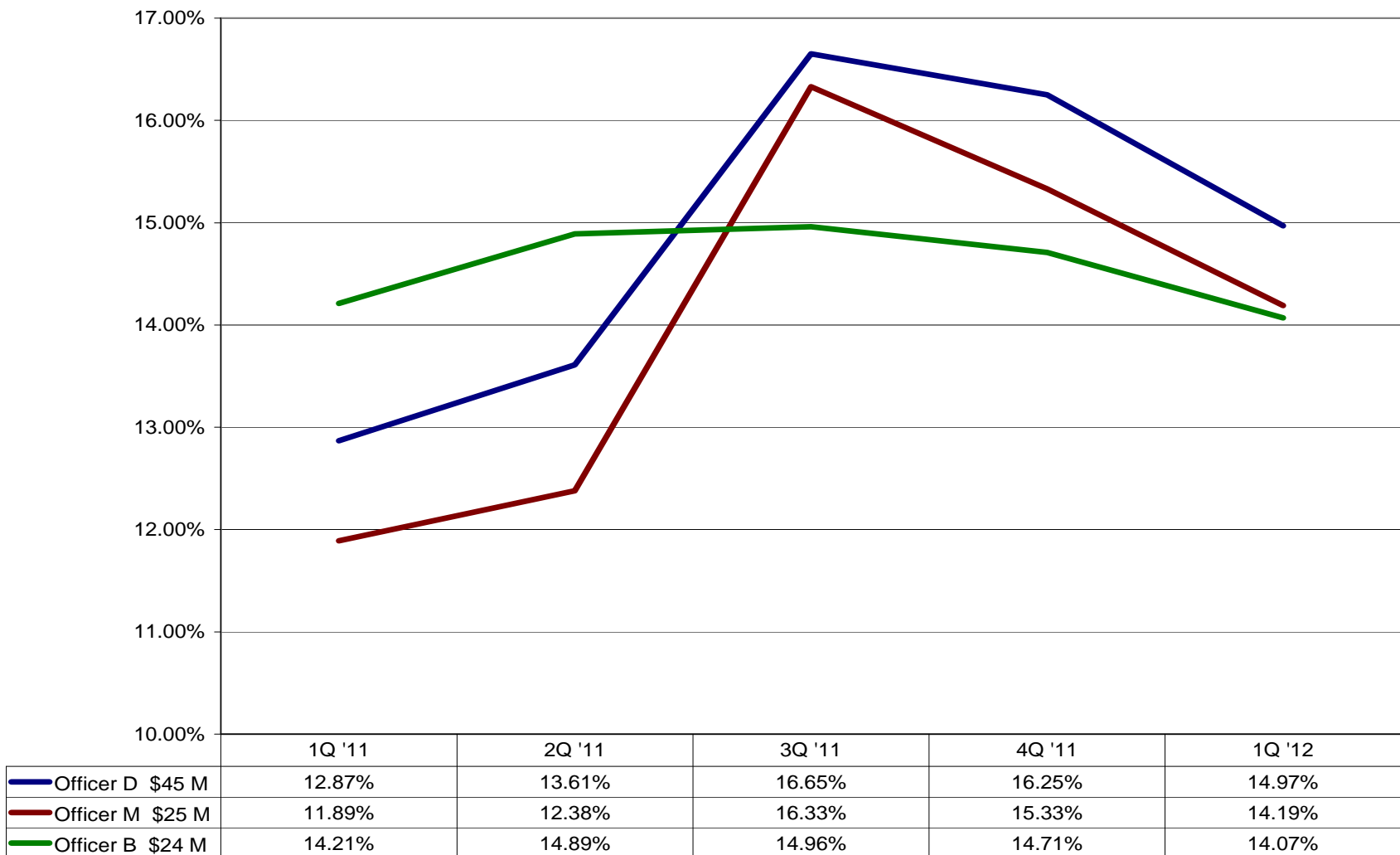
Landmark National Bank

ROE Report by Officer – Customer by Customer

- Enabled by Core Data Interface
- Customer's Ranked in Descending Order of **Relationship** ROE
- Applies to all Officers w/ \$2 M or more in Loans (16 Officers total)
- Tracks:
 - Average Loan Size
 - No. of Relationships
 - Yield %
 - Specific Provision Amounts
 - Profit by Customer
 - ROE by Officer

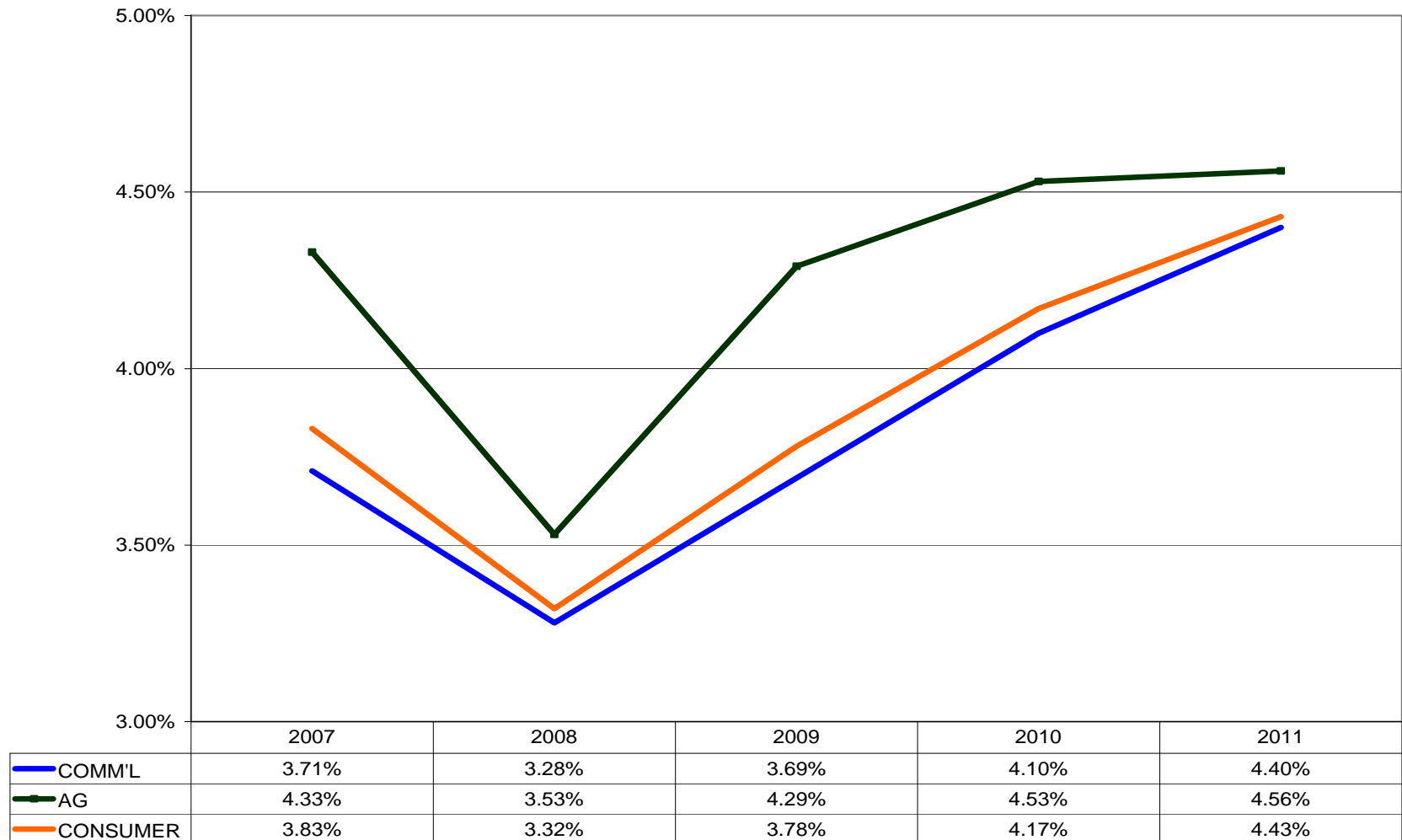
ROE Targets – Tracking by Officer

Landmark National Bank



A Recovery of Net Interest Margin

Landmark National Bank - (Net of FTP – Cost of Funding Loans)



Source: Austin Profitability System

ROE Trends – Actual Improvement Results

Landmark National Bank

As of June 30, 2011

\$226.5 M in Commercial Loans – Profit of \$2,524,056 – ROE = 7.96%

As of March 31, 2012

\$223.3 M in Commercial Loans – Profit of \$2,854,509 – ROE = 9.13%

Improvement in ROE = 14.7% 1.17%

Net Profit Impact

(\$223.3 M => Allocated Capital of \$31.3 M) **\$365,802**

Source: Austin ProfitabilitySystem – Tier II Analysis



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Administrative Tools

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Add New Grade

Select a Product

GRADE	DESCRIPTION	FACTOR		
1	PASS A - SUPERIOR - NO RISK	0.25	Edit	Delete
2	PASS B - ABOVE AVG CR - ACCEPT	0.50	Edit	Delete
3	PASS C - AVG CR - MANAGEABLE	1.00	Edit	Delete
4	PASS D - BELOW AVG CR - WATCH	1.50	Edit	Delete
5	SPECIAL MENTION	2.00	Edit	Delete
6	SUBSTANDARD	25.00	Edit	Delete
7	DOUBTFUL	50.00	Edit	Delete
8	LOSS	100.00	Edit	Delete

Loan Pricing System

Email Support New Feature



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Deposit Pricing System

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Loan Income Statement
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Loan Inputs
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System Config
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RESULTS ROA ROE Both # of Months to Summarize 60

Incl	Average Balance	Profit	ROA %	ROE %
<input checked="" type="checkbox"/> Loan 1	\$461,044.15	\$47,253.92	4.10%	14.64%
Loan 2	\$0.00	\$0.00	0.00%	0.00%
Loan 3	\$0.00	\$0.00	0.00%	0.00%
Others	\$0.00	\$0.00	0.00%	0.00%
Total	\$461,044.15	\$47,253.92	4.10%	14.64%

Benchmark Calculator

Run Calc on ROA Target ROE Target

Target Return % ROA ROE

Rate Required Solve Reset Calc

Fees Required Solve

Dep Bal Requ Solve for:

Customer New Loan Inputs

Loan 1 Loan 2 Loan 3 Include Loan Loan2

Loan Product Selection

Commercial Retail

Commercial

Loan Parameters

Loan Structure

Loan Amount (\$)

Fixed Rate (%)

Fixed Term

Adj Rate (%)

Reprice Frequency

Convert After:

Amort Per/Term Balloon months

Loan Comments:

Loan Fees (Non-Interest Income)

Provision, Credit Quality, Funding Cost

	%	\$	Frequency	Months	Monthly \$
Loan Loss Provision	<input type="text" value="0.000"/>	<input type="text" value="4500.00"/>	<input type="text" value="Up-Front"/>	<input type="text" value="1"/>	<input type="text" value="0.00"/>
Credit Quality	<input type="text" value="PASS B - ABOVE AVG CR - ACCEPT"/>				
Funding Option	<input type="text" value="US Treasury"/> <small>New yld curves updated 5/18/2012</small>				

Origination, Servicing, and Overhead Costs

Payment Structure

Customer Relationship Accounts

Loan Pricing System - Loan Input Screen - Windows Internet Explorer

https://www.austinassociates.com/FMS2_2/fmLoanPricing.aspx

File Edit View Favorites Tools Help

Loan Pricing System - Loan Input Screen

Loan Pricing System

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[Loan Cumulative Results](#)
[Loan Income Statement](#)
[Loan Rate Sheet](#)

Reporting
 Loan Inputs
 Results
[pdf](#) [Email](#)

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[Maintain Products](#)
[Funding Curves](#)
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RESULTS ROA ROE Both # of Months to Summarize 60

Incl	Average Balance	Profit	ROA %	ROE %
<input checked="" type="checkbox"/> Loan 1	\$461,044.15	\$45,768.92	3.97%	14.18%
Loan 2	\$0.00	\$0.00	0.00%	0.00%
Loan 3	\$0.00	\$0.00	0.00%	0.00%
Others	\$0.00	\$0.00	0.00%	0.00%
Total	\$461,044.15	\$45,768.92	3.97%	14.18%

Benchmark Calculator

Run Calc on: Loan 1 ROA Target ROE Target

Target Return: 15% ROA ROE

Rate Required: 5.1718% Solve Reset Calc

Fees Required: Solve

Dep Bal Req'd: Solve for: Non-Interest Bearing DDA

Customer: [Blank] Reset

New Loan Inputs

Loan 1 Loan 2 Loan 3 Include Loan copy Loan 2

Find Loan Save Reset Transfer Loan to Relationship

Loan Product Selection
 Commercial Retail
Commercial

Loan Parameters

Loan Structure: Fixed Rate

Loan Amount (\$): \$500,000.00 [Draw Schedule](#)

Fixed Rate (%): 5.000

Fixed Term: 60

Adj Rate (%):

Reprice Frequency:

Convert After:

Amort Per/Term: 240 Balloon 180 months

Loan Comments:

Loan Fees (Non-Interest Income)

Provision, Credit Quality, Funding Cost

	%	\$	Frequency	Months	Monthly \$
Loan Loss Provision	0.000	\$500.00	Up Front	1	0.00
Credit Quality	PASS C - AVG CR - MANAGEABLE				
Funding Option	US Treasury New yld curves updated 5/18/2012				

Origination, Servicing, and Overhead Costs

Payment Structure

Customer Relationship Accounts

Internet | Protected Mode: Off 100%

Loan Pricing System - Loan Input Screen - Windows Internet Explorer

https://www.austinassociates.com/FMS2_2/fmLoanPricing.aspx

File Edit View Favorites Tools Help

Loan Pricing System - Loan Input Screen

Loan Pricing System

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[Loan Cumulative Results](#)
[Loan Income Statement](#)
[Loan Rate Sheet](#)

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 Loan Inputs
 Results

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[Credit Factors](#)
[System Config](#)
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RESULTS ROA ROE Both # of Months to Summarize 60

Incl	Average Balance	Profit	ROA %	ROE %
<input checked="" type="checkbox"/> Loan 1	\$461,044.15	\$44,283.92	3.84%	13.72%
Loan 2	\$0.00	\$0.00	0.00%	0.00%
Loan 3	\$0.00	\$0.00	0.00%	0.00%
Others	\$0.00	\$0.00	0.00%	0.00%
Total	\$461,044.15	\$44,283.92	3.84%	13.72%

Benchmark Calculator

Run Calc on: Loan 1 ROA Target ROE Target

Target Return: 15% ROA ROE

Rate Required: 5.2682% Solve Reset Calc

Fees Required: Solve

Dep Bal Req: Solve for: Non-Interest Bearing DDA

Customer: [Blank] Reset

New Loan Inputs

Loan 1 Loan 2 Loan 3 Include Loan copy Loan2

Find Loan Save Reset Transfer Loan to Relationship

Loan Product Selection
 Commercial Retail
Commercial

Loan Parameters

Loan Structure: Fixed Rate

Loan Amount (\$): \$500,000.00 Draw Schedule

Fixed Rate (%): 5.000

Fixed Term: 60

Adj Rate (%):

Reprice Frequency:

Convert After:

Amort Per/Term: 240 Balloon 180 months

Loan Comments:

Loan Fees (Non-Interest Income)

Provision, Credit Quality, Funding Cost

	%	\$	Frequency	Months	Monthly \$
Loan Loss Provision	0.900	4500.00	Up-Front	1	0.00
Credit Quality	PASS D - BELOW AVG CR - WATCH				
Funding Option	US Treasury View yld curves updated 5/18/2012				

Origination, Servicing, and Other Fees

Payment Structure

Customer Relationship Accounts

Internet | Protected Mode: Off 100%

Example Risk Based Pricing – No Deposits

Landmark National Bank

Example Loan / Relationship - - Target ROE = 15%

\$500 K CRE Loan – Fixed Rate for 5 Years – No Deposits – No Fees

Credit Score 2 – “B” – 5.08% - No Risk Premium

Credit Score 3 – “C” – 5.17% - Risk Premium = 9 Basis Points

Credit Score 4 – “D” – 5.27% - Risk Premium = 19 Basis Points

Loan Pricing System

Email Support New Feature



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RESULTS ROA ROE Both # of Months to Summarize: 60

Incl	Average Balance	Profit	ROA %	ROE %
<input checked="" type="checkbox"/> Loan 1	\$461,044.15	\$45,768.92	3.97%	14.18%
Loan 2	\$0.00	\$0.00	0.00%	0.00%
Loan 3	\$0.00	\$0.00	0.00%	0.00%
<input checked="" type="checkbox"/> Others	\$75,000.00	\$6,886.59	3.67%	61.21%
Total	\$536,044.15	\$52,655.51	3.93%	15.77%

Benchmark Calculator

Run Calc on: Loan 1 ROA Target ROE Target

Target Return: 15 % ROA ROE

Rate Required: **4.8336%** Solve Reset Calc

Fees Required: Solve

Dep Bal Req'd: Solve for: Non-Interest Bearing DDA

- Logout
- Applications**
- Profitability Reporting System
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 - Deposit Pricing System
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- Amortization Schedule
 - Loan Cumulative Results
 - Loan Income Statement
 - Loan Rate Sheet
- Reporting**
- Loan Inputs
 - Results
- pdf Email
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- Maintain Users
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- My Account**
- Change Password
 - Challenge Question

Customer: [Blank] Reset

New Loan Inputs

Loan 1 Loan 2 Loan 3 Include Loan copy Loan2

Find Loan Save Reset Transfer Loan to Relationship

Loan Product Selection

Loan Parameters

Loan Fees (Non-Interest Income)

Provision, Credit Quality, Funding Cost

	%	\$	Frequency	Months	Monthly \$
Loan Loss Provision	0.900	4500.00	Up-Front	1	0.00
Credit Quality	PASS C - AVG CR - MANAGEABLE				
Funding Option	US Treasury view yld curves updated 5/18/2012				

Origination, Servicing, and Overhead Costs

Payment Structure

Customer Relationship Accounts

Select a Product to Add: Non-Interest Bearing DDA Add Historical Rates Amortizing Balance Calculator

Include	Product*	Balance \$	Credit %	COF %	Annual NII	PFL %	Orig Exp	Annual VE	Annual FE	Capital %
<input checked="" type="checkbox"/>	Non-Interest Bearing DDA	\$75,000.00	3.30%	0.00%	\$0.00	0.00%	\$92.68	\$81.60	\$288.02	3.00%

Loan Pricing System
[Email Support](#) [New Feature](#)

 Current User - jef

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RESULTS ROA ROE Both # of Months to Summarize

Incl	Average Balance	Profit	ROA %	ROE %
<input checked="" type="checkbox"/> Loan 1	\$461,044.15	\$45,768.92	3.97%	14.18%
Loan 2	\$0.00	\$0.00	0.00%	0.00%
Loan 3	\$0.00	\$0.00	0.00%	0.00%
<input checked="" type="checkbox"/> Others	\$625,000.00	\$23,901.13	1.53%	25.49%
Total	\$1,086,044.15	\$69,670.05	2.57%	16.73%

Benchmark Calculator

Run Calc on: ROA Target ROE Target

Target Return: % ROA ROE

Rate Required:

Fees Required:

Dep Bal Req'd: Solve for:

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Customer:

New Loan Inputs

Loan 1 Loan 2 Loan 3 Include Loan Loan2

[Find Loan](#) [Transfer Loan to Relationship](#)

Loan Product Selection

Loan Parameters

Loan Fees (Non-Interest Income)

Provision, Credit Quality, Funding Cost

	%	\$	Frequency	Months	Monthly \$
Loan Loss Provision	<input type="text" value="0.900"/>	<input type="text" value="4500.00"/>	<input type="text" value="Up-Front"/>	<input type="text" value="1"/>	<input type="text" value="0.00"/>
Credit Quality	<input type="text" value="PASS C - AVG CR - MANAGEABLE"/>				
Funding Option	<input type="text" value="US Treasury"/> view yld curves updated 5/18/2012				

Origination, Servicing, and Overhead Costs

Payment Structure

Customer Relationship Accounts

Select a Product to Add: [Amortizing Balance Calculator](#)

Include	Product*	Balance \$	Credit %	COF %	Annual NII	PFL %	Orig Exp	Annual VE	Annual FE	Capital %	
<input checked="" type="checkbox"/>	Money Market DDA	\$500,000.00	0.80%	0.50%	\$0.00	0.00%	\$46.34	\$40.80	\$144.01	3.00%	Edit Delete
<input checked="" type="checkbox"/>	Trust Fees	\$0.00	0.00%	0.00%	\$6,000.00	0.00%	\$500.00	\$1,200.00	\$2,500.00	0.00%	Edit Delete
<input checked="" type="checkbox"/>	Non-Interest Bearing DDA	\$125,000.00	3.30%	0.00%	\$0.00	0.00%	\$92.68	\$81.60	\$288.02	3.00%	Edit Delete

Example Risk Based Pricing – W/ Deposits

Landmark National Bank

Example Loan / Relationship - - Target ROE = 15%

\$500 K CRE Loan – Fixed Rate for 5 Years – No Deposits – No Fees

\$75 K in NIB – DDA

Credit Score 3 – “C” – 4.83% - Discount for Deposits = 25 Basis Points

\$625 K in NIB – DDA, with \$6,000 in Trust Fees

Credit Score 3 – “C” – 4.53% - Discount for Deposits = 53 Basis Points

Austin Associates, LLC.

Q & A

Increasing Loan Portfolio Profitability in a Slow Growth Environment: A Live Webinar Presented by Austin Associates, LLC

Presenter Biographies:

A former chief financial officer of a \$400 million service organization, Mr. Morris joined Austin Associates' Financial Management Division in 1998. He is responsible for profitability analysis services and works with clients who utilize the firm's innovative software products including its proprietary organization/product/customer profitability software and its loan and deposit pricing software. With over 25 years experience in various financial management roles, Mr. Morris also works with clients on strategic and operational planning, quality improvement, information systems, benchmarking and profitability improvement. A certified public accountant, Mr. Morris earned a Bachelor's degree in Accounting from the University of Toledo and an MBA from Northern Illinois University.

Jeffrey Morris



Michael E. Scheopner has served in key credit and lending capacities for more than 16 years with Landmark Bancorp, a \$600 million publicly traded company headquartered in Manhattan, Kansas. In his current capacity as Executive Vice President, Chief Risk Manager and Chief Lending Officer, he is responsible for all aspects of lending, credit administration and risk management encompassing commercial, real estate and consumer loan functions. In his role as a member of the executive management team, the bank's loan portfolio has grown to more than \$300 million through a combination of well-executed organic growth strategies and acquisitions.

Michael Scheopner



Financial Management Partners – Contact Us

➤ Asset / Liability Management Services



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