

Daily Business REVIEW

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February 23, 2004

www.DailyBusinessReview.com

The money merry-go-round

SOUTH FLORIDA COMMUNITY BANKERS GRASP FOR \$1 BILLION IN ASSETS BUT SOME MAY SWITCH HORSES SHORT OF THE BENCHMARK

by **Peter Zalewski**

Miami banker Joseph Guerra gets a cold call every other month or so from investment bankers who ask him if UniBank is ready to sell.

Guerra, the bank's chief executive, has always said no, but he is not so sure what his answer will be the next time he gets one of those inquiries.

Times are changing at UniBank as its assets near the \$500 million mark — the last major milestone for a community bank on its way to the coveted \$1 billion mark.

UniBank is one of nine South Florida-based banks at the same juncture. They must decide whether to forge ahead to the \$1 billion mark in assets or sell out. And the high premiums banks are fetching may be too much for shareholders to resist.

UniBank shareholders realize their days of being part of a small, community bank in South and Central Florida are ending and it is time to decide its future.

"When you get to a certain plateau, you have to grow," said Guerra, who as UniBank's president and chief executive has grown assets from \$66 million in 1993 to \$458 million in 2003. "Banks are in the business of leverage."

Seven South Florida institutions, such as Gibraltar Bank in Coral Gables and Sunrise-based

Union Bank, have passed the \$500 million asset mark and have their sights set on the billion-dollar benchmark. If they succeed, they will join another eight banks, including BankAtlantic and BankUnited, already well beyond the threshold.

For community bankers getting to the billion-dollar mark is important for both business and reputation reasons. In addition to feeding their egos, reaching the asset benchmark brings with it economies of scale and regulatory benefits.

The larger asset base also increases a bank's lending limits, giving it more freedom and ability to offer more lucrative commercial products such as construction loans and mezzanine financing for large real estate projects.

Not all these banks will make it to the billion-dollar goal. Many will sell and others will falter. But with so many institutions sharing the same ambition, the question arises: What does it take to be a \$1 billion bank in South Florida?

Billion-dollar benchmark

Like contestants on the famed game show "Who Wants to be a Millionaire" South Florida's community bankers are faced with great opportunities but just as many risks.

As in the game show, community bankers who find the right advisers to help them manage the process

stand a better chance of overcoming the obstacles and securing their riches and industry prestige.

Added credibility comes for those bankers who can create a \$1 billion institution. And once they attain the benchmark, these bankers can leverage their reputations to raise money to start or buy other banks.

For those bankers who fail and see their institutions stumble, chances are high that they'll find themselves looking for work. And the scrutiny these bankers face from shareholders and regulators is unlike any other industry.

For example, Advantage Bank of North Palm Beach gave in to demands from regulators for a change in control in July, after the 3-year-old institution failed to turn a profit.

A trio of well-established local bankers — Rudy Schupp, Warren Orlando and John Marino — raised enough money to buy a controlling interest in Advantage and infuse the struggling financial institution with much-needed cash. They also changed the name to 1st United Bank, the same name as an institution Orlando and Marino built to \$1 billion before selling to Wachovia in 1997.

"We are starting over," said Schupp, 1st United's chief executive, who grew Republic Security Bank from a one-trailer branch into a \$3.5 billion institution before selling it to Wachovia Bank in 2001. "We have a

lot of confidence but we are humble enough to know it is tricky."

Community banks trying to get on the rapid-growth track must deal with four critical areas: capital funding, growth strategy, management and regulator relationships. And the faster a bank wants to grow, the more intense these issues become.

Capital is considered the most crucial element, providing the financial fuel to operate and make loans. In basic terms, the more money a bank has, the larger the loans it can make and the more money it can earn. Adequate amounts of capital also allow banks to absorb the losses from a bad loan or failed business venture.

Capital levels affect the speed at which a bank can open branch locations in targeted neighborhoods.

Privately held banks also have to be smart with the amount they raise from their investors, because most community banks find it challenging to attract more than two rounds of investment, said Schupp, who raised \$5 million in two private rounds to start Republic Security.

After two rounds of funding, a bank often must go public to secure additional capital, as Schupp did with Republic Security less than two years after it started.

"To go beyond a couple of rounds of private equity capital raising usually proves difficult because you pretty much identified and talked to those that you know who would be

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interested in investing," he said. "It gets hard to do a third round."

One bank that may prove to be an exception to the rule is Miami-based U.S. Century Bank, the best-funded de novo bank in Florida history. Despite being in only its second year, the bank has raised \$60 million from a small group of wealthy and powerful local investors.

It is preparing to use some of that money to open eight branches, and is scouting out an additional seven sites. The capital infusion has also boosted U.S. Century's lending limits to \$13.6 million for a single client, allowing it to finance bigger deals. This is driving assets, which totaled \$207 million on Jan. 31.

"We are a little more aggressive in terms of building a branch network," said Octavio Hernandez, president and chief executive of U.S. Century Bank. "Some of the other banks feel they want to grow their headquarters first, and little by little start branching out. We take a little bit different approach."

U.S. Century plans to use the capital to expand into Broward and Palm Beach counties next year after building its Miami-Dade County footprint. Despite its considerable war chest, the bank is opting for the cheapest way to quickly expand its network, leasing vacant branch locations rather than acquiring land and building.

On average, bankers say it costs just \$1 million to start a new branch in a leased location, compared with \$3 million to build a branch from scratch.

Managing growth

U.S. Century also has enough money to realistically look at buying a bank of similar size, giving it yet another option for achieving rapid growth.

Mergers and acquisitions can play a critical role in reducing the time required for a bank to reach its quest for \$1 billion. Bankers refer to it as the buy-versus-build strategy. If done right, a bank can quickly grow its market share in targeted neighborhoods.

The strategy works well for acquiring banks if they are run by managers with experience in integrating financial institutions.

But the value of an acquired bank can be quickly diminished if key executives are not retained.

Alabama-based Colonial Bank experienced just that when it paid \$106 million for Palm Beach National Bank & Trust in 2002. Shortly after the acquisition, dozens of vital Palm Beach National



Octavio Hernandez as president and CEO of U.S. Century Bank heads the best-funded de novo bank in Florida history.

employees left and took their clients with them. Colonial Bank responded with a lawsuit last month against several former employees of Palm Beach National's trust division. Colonial accused them of breaking their fiduciary duty by recruiting coworkers to switch to a different institution and take their books of business with them.

Some banks have opted for a slower path to the billion-dollar benchmark. They utilize a more grassroots approach, opening one branch at a time and growing it by staffing it with locals and getting involved in the community. The costs and risks are lower, but it takes longer for the branch to become profitable.

Union Bank of Florida, which was founded in 1971, has grown its assets to \$859.3 million using the just that approach.

It has opened 10 branches in the past five years, pushing its total to 18. Assets have also tripled during the same time.

Union Bank, whose main shareholders include Lennar chief executive Stuart Miller, probably won't surpass the \$1 billion milestone until the second quarter of this year. But the institution has already establishing a new goal for itself — \$5 billion in assets by 2008.

"I think it is going to be just as challenging, because the competition is heating up, economies are constantly changing, our markets are continuously changing," said Lynne Wines, president and chief executive of Union Bank. "But it shouldn't take us 32 years, which is what it took us to get to \$1 billion."

Top guns

As an institution increases its assets and branches, the business changes and the bank will need the right management to stay on track. Sometimes the mix of managers needs adjustment.

Boca Raton-based Pointe Bank, for example, hired a longtime

Miami-Dade County banker in December in an effort to get its commercial lending services in Miami onto a faster growth track.

Charles Umberger, Coconut Grove Bank's former president, joined Pointe Bank on Dec. 15 to help it achieve its goal of doubling assets from \$384 million within three years.

In some cases though banks need to completely overhaul management, not just bring in executives with particular skills or experience.

Boca Raton's First Southern Bank wants to increase its \$271 million in assets to \$500 million within three years and \$1 billion by 2008. To accomplish that, First Southern is hiring a management team with extensive experience running institutions with assets 10 times larger than its current level.

Six of its top nine management hires have come from much larger institutions, including SouthTrust Bank, Fleet Bank and BankAtlantic. Five of the bank's seven branch managers are from institutions such as Citibank and SunTrust.

Bank president and chief executive Peter Mottek joined First Southern in 2001 after a 17-year career with Citibank. Another longtime Citibank executive, Donald Kafka, joined First Southern in March 2003 after a 20-year career with America's largest bank.

First Southern's executives hope to grow the bank's assets by 20 percent annually by utilizing their experience to attract more business from the rapidly expanding companies in Palm Beach and Broward counties.

"It's all management," said Brian Sherr, chairman of First Southern Bank. "I would think to really be excellent, you need excellent management."

First Southern still has a long way to go, but it has made great strides toward regaining its financial footing since it ran into trouble in 2000. A \$7 million loan went bad after a borrower filed for bankruptcy protection.

But since then, First Southern is profitable and its financial performance is improving after losing money in 2000 and 2001. The bank's return on assets climbed to 0.56 percent on Sept. 30 after slipping with the loan charge-offs to a negative 0.68 percent in 2000. The industry norm is 1.2 percent.

Bad loans, questionable loan underwriting and uncontrolled rapid growth are three issues that bank regulators watch for in banks, especially the smaller ones trying to aggressively build a franchise.

Bad loans are difficult to justify,

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but loan-application procedures and rapid growth can be explained if regulators have confidence in a bank's executive management and understand the institution's business plan. It also helps if a bank is well-capitalized to absorb any mistakes, and making a profit, said Miami banking analyst Ken Thomas.

"Fast growth is a red flag that attracts regulators because it can suggest that they are paying high [interest] rates" for deposits, Thomas said. "It isn't necessarily bad if you can support the fact you are going to bring in good money."

South Florida's growing population and diversifying economy offers plenty of opportunities for banks to lend out low-cost deposits. The net interest margins on these loans can be lucrative for banks.

The rapid population growth makes South Florida an attractive market for both community and larger national banks. And because these national banks have such a big share of the local deposit base, experts say South Florida is ripe for more large community banks with assets in the billions. Their growth would come at the expense of national banks such as Bank of America and Washington Mutual, which have a considerable presence in the tricity area.

"The business is there, and they can coexist in the market, in my mind, without question," said 1st United's Schupp. "It is a question of, can [community banks] navigate the course toward \$1 billion in size and do they want to?"

Many banks may have the desire, but not all will reach the billion-dollar milestone.

"Having seen community banks now for over 15 years, I will tell you that some of them will not make it," he said. "That is just the way it works. You can stall. If your asset quality is not good you can have a problem. When those problems blow up, it disrupts the best-laid plans. It takes capital to continue."

Shareholders wanting to cash out on their investments can also affect the strategic planning of bank management. Community banks have a responsibility to alert shareholders of every offer they receive, regardless of what the management thinks. These offers normally come in more frequently once a community bank's assets surpass \$500 million in assets.

UniBank's assets totaled \$458 million on Sept. 30, pushing closer to the \$500 million threshold.

UniBank's Guerra won't be the one making the decision if the 24-year-old bank will sell because he is only a minor shareholder.

That decision rests with Unibank's majority shareholder, the Fonalledas family of Puerto Rico, which owns 90 percent of the bank's stock. The family operates a food products company and has extensive real estate holdings on the island.

UniBank's board members began

discussing the bank's future in November but set no deadline for a decision. Guerra expects it come within the next six months.

He said UniBank has the foundation of capital, growth plans, managers and a good relationship with regulators that could allow it to become a \$1

billion bank. Still, it's not his decision.

"We have to have the major stockholder in agreement," Guerra said. "I imagine they have been discussing plans as to what will be done because it is their money. They will have to make the decision soon, one way or another." ♦

Billions-dollar club

Fifteen locally operated banks hope to reach \$1 billion in assets in the next decade. The banks (ranked by current total assets) are listed below and the year they project to hit their \$1 billion target.

Bank	Assets (in millions) *	Target year
International Bank of Miami **	\$986	2003
Union Bank of Florida	\$859	2004
Kislak National Bank	\$835	2004
Commercial Bank of Florida	\$774	2005
Gibraltar Bank	\$694	2006
BAC Florida Bank	\$662	2006
TotalBank	\$554	2007
Espirito Santo Bank	\$512	2007
UniBank	\$459	2007
Pointe Bank	\$384	2009
First Southern Bank	\$271	2008
Metro Bank of Dade	\$224	2013
U.S. Century Bank	\$207	2009
PanAmerican Bank	\$170	2009
1st United Bank	\$54	2014

Locally operated banks that have at least \$1 billion in assets.

Bank	Assets (in billions)
BankUnited	\$7.1
BankAtlantic	\$4.7
Ocean Bank	\$4.3
Commercebank	\$3.1
Fidelity Federal Bank & Trust	\$2.9
City National Bank of Florida	\$2.3
Mellon United National Bank	\$1.8
Lydian Private Bank	\$1.0

* As of Sept. 30, 2003

** International Bank of Miami's assets are estimated to have reached \$1 billion since the most recent figures were released.

Sources: Financial institutions, FDIC