THE FINDLEY REPORTS

BANKING NEWSLETTER AND DIRECTORS' COMPASS

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Editor's Comments

UNCHARTERED WATERS

March was the month where financial institutions entered into uncharted waters. It was a time of great challenge and uncertainty with the COVID-19 pandemic, unprecedented drops in interest rates, shelter in place, and a significant drop in stock market values. When we enter into uncharted waters, much like we did 10 years ago, we know this causes anxiety in community bank board rooms, C-suites, and throughout the organization, inclusive of shareholders, depositors, borrowers, staff, and community.

As we navigate these uncharted waters, we need to focus on what we know and not overreact. As we have written in the past, immediate short-term reactions by bankers that are not well thought out often cause more problems in the long-term, but, what we have also experienced, is a coming together of our country, our communities, our bankers, and our regulators to help each other in these uncharted waters. What we also know in viewing the year-end call reports is that the vast majority of community banks have stable balance sheets with strong capital levels that will be able to withstand the ups and downs of the economy; what we refer to as a fortress type balance sheet. We also know that income levels, although they have been impacted due to the compression are still positive for most.

The talent level at our community banks is excellent, and there is commitment and connection to the communities they serve. Regulatory relationships are the best they have been in many years, and the regulatory agencies are reaching out to our banks to see what they can do to make it easier for our community banks to navigate these uncharted waters.

While stock prices have fallen, we continue to remind our boards and managements that it is not the sale of a few thousand shares that reflect the true value of our community banks. Focus on ROAA, ROAE, EPS core deposits, quality loan portfolio, and efficiency ratios. Even with the expected drop in net income in 2020, these ratios are still very good and reflect the true value of our community banks. While we do think that the COVID-19 pandemic, the shutdown, and the significant drop in interest rates will impact some of borrowers, we must be able to work with our borrowers. The guidance from the regulators is appreciated, but the community bankers have the boots on the street. There will be some choppiness over the next several months, but we can get through this. We believe that at the end we will be stronger for it. Although our returns will not be as great as what we had anticipated going into 2020, possibly our returns will be better in the sense that we are better people and we have better community banks.

This month's "Directors' Compass" focuses on a book written by Kevin Brown called, *The Hero Effect*. We do need a hero, and we need it now! We believe that community bankers cannot just be leaders but have to be heroes within our communities, showing strength to everyone who touches their bank.

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SPECIAL POINTS OF INTEREST:

- *Recognizing Performance*
- *Regulatory Relief and What it Means*
- *First Glance 12L - 4th Quarter 2019*

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OUR 52ND YEAR OF BANKING PUBLICATIONS

UNCHARTERED WATERS

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On behalf of all *The Findley Companies* and in association with California Community Banking Network, we remain ready to counsel and help in any way our community banks. While we remain sheltered in place, let's still remember that we still need to connect with others. If we take the position that we are in it all together, and we are here to help everyone get through this, then we know that we can. We stand true to the virtues of *The Findley Companies*, which we have espoused in the past as loyalty, courage, honor, and compassion. Staying true to these virtues allows us to definitively sail through uncharted waters. While it will be bumpy, we should be safe.

A WHITE-KNUCKLED RIDE

March has been a white-knuckled ride for most financial institutions, as we have seen the Federal Reserve significantly lower interest rates 150 basis points in reaction to the Coronavirus pandemic. This has resulted in several analysts expecting that there will be some significant headwinds on all financial institutions with regard to profitability in 2020, and also some underlying issues with regard to borrowers. There will be a significant headwind, but at the same time, most banks will navigate through this challenge.

With all of this, the federal regulators have repeatedly stated that the financial system is able to manage the COVID–19 pandemic. While we may well be in a recession, it is expected to be a short one, since the fundamentals of the economy have been so strong.

RECOGNIZING PERFORMANCE

The April *Newsletter* is always the time in which we recognize the *Super Premier*, *Premier*, and *Commendable* performing banks for their performance the previous year. While we recognize that all financial institutions are having some challenges in 2020, it is still important to recognize performance in 2019. We are thrilled that there were 104 banks recognized for 2019 performance by *The Findley Reports*. There were 76 *Super Premier* performers, 14 were *Premier* performers, and 14 *Commendable* performers.

Why is this relevant at this time? It's relevant because when we look at the balance sheets and income statements, as well as the performance levels for these banks in 2019, we are confident that the vast majority will be able to sail these uncharted waters. This is great news and demonstrates the health of the community banks and the ability to move forward in the challenges with 2020.

The final list of *Super Premier* and *Commendable* performance is contained as insert to this month's *Newsletter*. There were a few banks that we added to the list due to Editor's discretion. For the most part, all of the banks had the performance numbers to receive their ranking.

While we have finished off 2019, we also recognize that 2020 is a new day based upon all of the challenges that are facing our banks. As we look to Premier performers for 2020, we have significantly recast the numbers that we initially came out with earlier this year. Also included in this *Newsletter* are the criteria as modified for *Super Premier* and *Premier* performing banks for 2020.

As we have always stated, *The Findley Reports* attempts to be fair with recognition of our community banks for their performance, and we believe that the 2020 criteria as reconstituted is fair. However, we will again take a look at it based upon the economic challenges our banking environment will be facing in 2020. Possibly in 2020 we will be recognizing all banking institutions that really make a difference from the standpoint of giving back to their communities, connecting to their depositors and borrowers, and staying true to their staff.

While we always looked at the *Super Premier*, *Premier*, and *Commending* performing as objective numbers for performance, we actually think that there will be many banks that may not make any money in 2020, but have truly made a difference. We think some level of net income is important, but we will also take into consideration some intangible factors for a few that make little if no money in 2020, but really connect to their community and make a difference. They are also worthy of additional recognition.

RECAST 2020
SUPER PREMIER PERFORMING,
PREMIER PERFORMING, and
COMMENDABLE PERFORMING CRITERIA

The following are criteria for the ratings of ***Super Premier Performing Bank*** and ***Premier Performing Bank*** at December 31, 2020:

For C Corporation Banks -		
	SPB	**PPB**
Growth (% of Beginning of the Year Totals) Increase in either Gross Assets, Total Deposits, Total Loans or Gross Income	**2.00+**	**0.00+**
Net Operating Income (% of Average Gross Assets) Before Taxes and Reserves	**0.80+**	**0.40+**
Net Loan Loss (% of Beginning Gross Loans)	**0.80-**	**1.00-**
Equity Return (% of Beginning of the Year Total Equity Capital) Beginning Capital Over 10% Average Leverage Capital	**6.00+** **5.00+**	**4.00+** **3.00+**
****Must Maintain "A Quality"***		
For S Corporation Banks -		
Growth, Net Operating Income, and **Net Loan Loss** criteria are the same as for C Corporations.		
Equity Return (% of Beginning of the Year Total Equity Capital) Beginning Capital	**8.00+**	**6.00+**
***		
Commendable Performing Bank must attain 3 of the 4 Premier Performing criteria.		
***		
To meet the criteria for Super Premier, Premier, or Commendable Performing Bank, the bank must also meet the Findley Reports A-Quality Criteria which appear on the following pages.		

REGULATORY RELIEF AND WHAT IT MEANS

In March, the FDIC issued several financial institution letters encouraging financial institutions to take prudent steps to assist customers and communities affected by COVID-19. The FDIC recognizes that the efforts to work with customers and communities can be consistent with safe and sound banking practices and in the public interest.

The FDIC issued guidance for community banking institutions that are less than $1 billion. The highlights of the guidance encourage financial institutions to work with customers and companies affected COVID-19 in a prudent manner, and to understand that they're uniquely involved in a situation that could include significant temporary business disruptions and challenges. The FDIC encourages financial institutions to work with all borrowers, especially borrowers from the industry sectors particularly vulnerable to the volitivity in the current economic environment, small businesses and independent contractors that rely on affected business industries. Financial institutions should take prudent efforts to modify the terms on existing loans to affected customers, which will not result in examiner criticism. The FDIC will work with affected financial institutions to reduce burden when scheduling examinations, including market making great use of the offsite reviews consistent with applicable legal and regulatory requirements.

We appreciate the words from the FDIC, and the CARES Act takes this further related to the modifications to credits without a designation of a troubled debt restructure ("TDR.") This also means that the accountants will get onboard with regard to how to handle the accounting for TDR-related matters. We believe that working across the board with borrowers to provide some interest and principal relief is a good thing.

The SBA also sent out an information notice reminding lenders of their unilateral authority to provide temporary relief in the form of deferred payments to existing borrowers under certain circumstances. The breakdown of the 7A business loans and 504 business loans which affect so many of our financial institutions should be evaluated.

We also know that the regulatory agencies have been asking community banks for additional steps. We believe that some of these additional steps should include: the elimination of the interest rate cap restrictions for all financial institutions eliminating the well-capitalized requirement that should provide liquidity opportunities for bank institutions; rescheduling of examinations; reinstatement of TAG; and deferral with regard to asset quality downgrades. As we have stated before, this is uncharted waters for the regulatory agencies and our financial institutions, and it is time that we all work together on a common-sense approach. We believe that the tools are there for all parties to make this work. All indications are that a collective effort is underway.

TAX FILING DELAY

Some good news out of all of this is that the Federal government postponed the deadline for filing federal income tax to July 15, 2020 from April 15, 2020. This gives all taxpayers and businesses additional time to file and make payments without interest or penalties. However, we encourage those taxpayers with potential tax refunds make their filings as soon as possible in order to get money in their hands.

CALL REPORT GRACE

On March 25, 2020, the FDIC, along with the other federal banking agencies that are members of the Federal Financial Institutions Examination Council (FFIEC), issued a press release recognizing that financial institutions may need additional time to submit certain regulatory reports in light of the adverse effects of COVID-19. Consistent with the FFIEC release, the FDIC will not take action against any institution for submitting its March 31, 2020, Consolidated Call Reports after the official filing deadline, provided the report is submitted within 30 days thereof.

In addition, the Federal Reserve will not take action against a financial institution with $5 billion or less in total assets for submitting its March 31, 2020, Consolidated Financial Statements for Bank Holding Companies (FR Y-9C) or (FR Y-11) after the official filing deadline, as long as the applicable report is submitted within 30 days of the official filing due date.

FIRST GLANCE 12L – 4TH QUARTER 2019

The Federal Reserve Bank of San Francisco ("FRBSF") issued the *First Glance 12L* for the 4th quarter of 2019 in early March. The title is, *COVID-19 Fears Could Amplify Bank Earnings Pressure*. While this is a little dated, we believe that its excellent information for board and managements. Some of the takeaways with regard to 4th quarter information: job growth in the West remained robust; housing markets diverged across the district as the decline in mortgage rates paused; commercial real estate fundamentals in the district remain stable; investors became more optimistic about the future conditions; bank earnings dipped year over year and quarter over quarter primarily due to the NIM compression; annual net loan growth down shifted further but loan defaults and losses remained low; balance sheet liquidity and capital positions improved slightly; and supervisory rating upgrades continue to outpace downgrades. What is relevant is that going into COVID-19 and the challenges of the end of the 1st quarter and 2nd quarter of 2020, the overall fundamentals of the financial institutions are solid.

Some of the hot topics that were set forth in the *First Glance 12L* include that optional alternative capital measures will be reported by community banks beginning in the 1st quarter of 2020. The CBRL should simplify capital calculations and reduce reporting and compliance burdens. The majority of community banks in the District are expected to qualify for CBRL. CBRL adoption should increase credit and liquidity risk profiles, and CBRL qualifications could shift during the recession. Additional hot topics are cyberthreats continuing, especially in the COVID-19 situation; Bank Secrecy Act; Anti-Money Laundering compliance remains a focus of all of the regulatory agencies; and real estate lending concentrations are still of concern. However, nonowner-occupied CRA loan concentrations have eased from pre-crisis peaks, because of lower C&LD lending volumes, but they remain above the US average among most district states. The quality of the loan growth is still a minor issue for a regulatory perspective; however, asset quality remains relatively strong. Also noted in the *First Glance 12L* is the global economic slowing and COVID-19.

While it is a bit dated, it provides a background of the stability of the financial institutions entering into these uncharted waters.

CRA CREDIT

There is some good news regarding Community Reinvestment Act compliance, as all of the federal regulators stated that banks may receive CRA consideration for helping customers weather the effects of the Coronavirus pandemic. All of the regulators have stated that they will look favorably at banks that adjust retail banking and lender activities to assist low- and moderate-income customers, small businesses, and small farms in the bank's assessment area. The regulators state that efforts by financial institutions to modify the terms on new or existing loans for affected customers, small businesses, and small farms to ease the financial burden of the outbreak will receive CRA consideration and not be subject to examination or criticism. All of the regulators stated this position will be effective for six months past the date when the Federal government's national emergency declaration is lifted, unless extended.

FDIC BUYOUTS

On March 5, 2020 the FDIC announced that its offering buyouts to roughly 20% of its current staff. It stated that it will be offering voluntarily retirement and early separation opportunities to help reshape the Agency's workforce and enhance preparedness. One wonders about the timing of this, especially with regard to the lockdowns and the recent actions taken by the Federal Reserve Board of Governors. "Today's announcement is part of a deliberate strategy to further reduce layers of management; acquire new skill sets and allow the agency proactively address succession planning prior to any crisis or emergency situation. This program will enhance our agility, preparedness, and technology transformations," stated FDIC Chair Jelena McWilliams.

The FDIC is downsizing due to a rapidly aging workforce. According to the FDIC, approximately 42% of the FDIC's workforce will be eligible for retirement in the next five years. I'm just curious on the time of this particular notice, and whether the FDIC will be slowing this. It also means that the FDIC thinks that the overall strength of the financial instructions is actually better. If they felt it there were weakness, they would be ramping up.

DELAYING CECL

In mid-March FDIC Chair McWilliams stated that the Financial Accounting Standards Board should postpone implementation of the current expected credit loss standard ("CECL") in light of the COVID-19. FDIC Chair McWilliams stated that the FASB should allow banks currently adopting CECL to have the option to postpone their implementation of the accounting standards, and that the FASB should impose a moratorium on the effective date of the implementation for banks that have yet to adopt CECL. FDIC Chair McWilliams expressed concern that the CECL may strain banks' ability to lend to customers and "the growing economic uncertainties stemming from the pandemic may make certain allowance assessment factors potentially more speculative and less reliable at this time."

At the end of March the federal regulators issued an interim final rule allowing banks to push out CECL for two years. Banks that have already adopted CECL have the option of choosing the three-year option contained in the 2019 CECL rule of the five-year option that includes the new two-year delay.

We believe that the FDIC is dead spot on, on this. In addition, we notice that the Conference of State Banks Supervisors has also issued a statement in support of the FDIC's position with regard to delaying the accounting rules. These are good steps.

FOREGOING STOCK REPURCHASES

We notice that several financial institutions announced that they are not moving forward with stock repurchases as this particular time. We also know that President Trump, at several of his press conferences, stated his opposition to stock repurchase programs at this particular time. This is a time where entities should be preserving capital as well as preserving liquidity as we go through these uncharted waters.

CFPB INDEPENDENCE

Earlier in March, the Supreme Court in the CFPB case began focusing on Presidential authority to fire the CFPB head, which was created by the Dodd-Frank Act in the wake of the financial crisis. The Supreme Court held oral arguments in early March 2020 to debate the CFPB's fate. We should expect some action by the Supreme Court over the next few months, but, who knows with COVID-19.

VIRTUAL MEETINGS

Recently, the Securities and Exchange Commission ("SEC") offered guidance to companies wanting to hold virtual proxy meetings or reschedule those gatherings and for shareholders to present their resolutions through alternative methods.

In the March 13, 2020 guidance, SEC staff noted that the ability of companies to conduct virtual meetings is governed by state law in each company's governing documents. The staff outlined notification of options for companies that decide to hold a virtual meeting or hybrid meeting, an in-person meeting that also permits shareholders to participate through an electronic means, or if the company decides to change the date and time of the annual meeting due to COVID-19.

Several entities are moving toward the virtual meeting; however, we are encouraging them to take a look at their bylaws. While virtual meetings are permitted in the State of California with some requirements, let's be certain that your bylaws have the appropriate language with regard to holding a virtual meeting. The fortunate part is that the bylaws dealing with this particular section can usually be amended by the Board of Directors and without shareholder approval. Also, there may need some clean-ups in California law related to the more stringent requirement of the virtual meeting process. We are advising most banks to wait a bit. Again, things are very fluid, so a wait-and-see attitude may be best.

While we have had several entities want to move forward with virtual meetings for 2020, we have also had several institutions postpone

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Editor's Comments

VIRTUAL MEETINGS

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their meetings. Postponement of the meeting is possible and permitted under California law; however, it must be called within 15 months of the previous meeting. This should give institutions plenty of time in which to structure their annual meeting. Fortunately, for most banks the annual meeting is only for the election of directors and the ratification of accountants. We are not seeing much change to this in 2020.

COMING TOGETHER AND KINDNESS

While all of us have been ordered to shelter in place, which on the face of it encourages isolation, we believe that this is a time where we need to come together, not necessary in social gatherings, but come together through electronic means, reaching out to others, and staying connected. This month's "Professional Corner" by Cary Baily-Findley deals with some tips with regard to building interactions in this challenging time. We encourage you to check in, stay connected, and be safe.

During the CCBN C-Suite Call on March 26, 2020 there were several suggestions on how to help customers as well as staff during this difficult time. After the call there were several other suggestions and points offered by bankers who listened in. One in particular was a bank using the purchase of gift cards as a means of supporting local restaurants. During this time, the board of this bank authorized $100,000 to be used to buy gift cards of $2,000 per local restaurants and bank clients. This is a way to help with cash flow and, at same time, the ability to continue to support important businesses. They plan to distribute these gift cards to staff and others affected. Simple act of kindness that will be returned multiple times; what can be referred to as a double positive!

Gary Steven Findley*, *Editor

FEDERAL AGENCIES ISSUE WHIRLWIND OF PROPOSALS, GUIDANCES AND RULES IN CONNECTION WITH COVID-19 PANDEMIC

Over the last few weeks, as the United States COVID-19 pandemic response heightens, the financial institution regulatory agencies have issued a myriad of releases aimed as assisting those institutions and their customers deal with the ever-changing circumstances. The following are just a few highlights of several of the issuances.

Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus

The agencies state that they will not criticize institutions for working with borrowers so long as they mitigate risk by using safe and sound practices. They also indicted they will not criticize institutions that work with borrowers "as part of a risk mitigation strategy intended to improve an existing non-pass loan." The agencies have confirmed with FASB that short-term modifications made on a good faith basis in response to COVID-19 to borrowers who were current prior to any relief, are not considered troubled debt restructuring ("TDR"). This would include short-term modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. If the modification is to provide temporary relief for current borrowers affected by COVID19, the institution may presume that a borrower who is current on payments is not experiencing financial difficulties at the time of the modification for purposes of TDR determination, and no further TDR analysis would be required. Further, regardless of whether modifications result in loans that are considered TDRs or are adversely classified, the agencies state that their examiners will not criticize prudent efforts to modify the terms on existing loans to affected customers. Also, efforts to work with borrowers of one-to-four family residential mortgages, where the loans are prudently underwritten and not past due or carried in nonaccrual status, will not result in the loans being considered restructured or modified for the purposes of their respective risk-based capital rules. Loans with deferrals granted due to COVID-19 as past due solely because of the deferral will not have to be designated as past due. The agencies note that during these short-term arrangements, these loans generally should not be reported as nonaccrual, qualifying this by further stating that "each financial institution should refer to the applicable regulatory reporting instructions, as well as its internal accounting policies, to determine if loans to stressed borrowers should be reported as nonaccrual assets in regulatory reports."

Federal Bank Regulatory Agencies Issue and Seeks Comment on Interim Final Rule for Money Market Liquidity Facility

The Federal Reserve Board, with the approval of the Secretary of the Treasury, is authorizing the Federal Reserve Bank of Boston to establish the Money Market Mutual Fund Liquidity Facility ("MMLF"), under which it will extend nonrecourse loans to eligible borrowers to purchase assets from money market mutual funds. Assets so purchased will be posted as collateral to the Federal Reserve Bank of Boston. Banking institutions would be eligible borrowers under the MMLF. Eligible collateral under the MMLF includes U.S. Treasuries and fully guaranteed agency securities, securities issued by government-sponsored enterprises, and certain types of commercial paper. The interim final rule allows banking institutions to neutralize the effects of purchasing assets through the program on their risk-based and leverage capital ratios. As participation in the MMLF will affect the balance sheet of a banking institution because the banking organization must acquire and hold assets on its balance sheet--the eligible collateral pledged to the Federal Reserve Bank, the institution could potentially be subject to increased capital requirements. Because of the nature of the extension of credit and the corresponding minimal risk, the agencies are excluding the effects of purchasing assets through the MMLF from a banking organization's regulatory capital. "Specifically, the interim final rule would permit banking organizations to exclude nonrecourse exposures acquired as part of the MMLF from a banking organization's total leverage exposure, average total consolidated assets, advanced approaches-total risk-weighted assets, and standardized total risk-weighted assets, as applicable.

The foregoing is a general discussion of the issuances and does not discuss all aspects thereof. This discussion is not a substitute for professional advice on a specific question. For further information, please contact Gary Steven Findley & Associates at (714) 630-7136.

WE NEED A HERO, NOW!

The first quarter of 2020, specifically the month of March, has tested everyone in this country. With the Coronavirus pandemic, the wild fluctuations of the stock markets, significant decreases in interest rates, the implementation of travel bans, shelter in place orders, five trillion dollars of quantitative easing from the Federal Reserve, media hysteria, shutdowns of schools and business for a period of time, and no sporting events or public areas of congregation -- we need a hero -- we need a hero, now!

In search of some words on how community bankers can be heroes, we read *The Hero Effect, Being Your Best When It Matters the Most,* a book written by Kevin Brown, Copyright August 2017, Keven Brown Enterprises, LLC/ Apple Pancakes Publishing.

Mr. Brown was recently a keynote speaker at the ICBA Annual Conference in Florida, and his words on how to be a hero, primarily as it relates to our community bankers, is quite practical. Community banks touch many parts of our communities, inclusive of shareholders, officers, employees, directors, borrowers, depositor, regulators and vendors, who we have traditionally referred to as our "partners."

As a time of uncertainty, this is a time where community banks need to step up, especially their leaders, and show strength and provide assurances to their partners that if we all act together and have the right frame of mind, we can get through these challenges, no matter how daunting they are. Community banks need not to just be leaders, they must be Heroes!

Over the years we've had the privilege of interviewing bankers and profiling community banks that we deemed "exceptional." When you look at what the banks are able to do and also what their leaders are able to accomplish, we can also deem them heroes, because they show the way, make a difference, and always have the tendency to make things better.

Mr. Brown states, "Heroes have this uncanny ability to show up larger than life. Larger than life means bigger than life's problems, bigger than the storyline that life gave us, bigger than the challenges that our clients and employees are facing." How true, and we need those heroes today. We need those heroes that can deal with the short-term problems with a long-term focus. Heroes that act for all and not just a select few. Heroes that don't overreact and look at things by trying to help others as compared to just themselves.

In *The Hero Effect,* Brown envisions a workplace where exceptional behavior takes precedence over the ordinary, where compelling vision aims to make life better for the whole community. Why not beyond the workplace to everywhere? This is a time where bank leaders need to think about and serve all partners, because creating a positive environment for all of the partners, inclusive of our employees and customers, creates a better environment for us all.

Brown describes in *The Hero Effect* his own take on heroism, when it transports the hero out of the realm of the mythology into the ordinary world. His H.E.R.O. is an acronym for: **h**elping (H), without strings attached, creating an **e**xceptional (E) experience, taking **r**esponsibility (R) for the actions, and seeing the world through the lens of **o**ptimism (O). His heroes make life better, solve problems and move people from where they are somewhere new. Sounds like many of our exceptional bankers and also where boards and managements need to be focusing. This is a time for leadership. This is a time for stepping up. This is a time for making a difference.

For those who do not want to do this, or do not have the courage or bravery to take the appropriate steps, we find that their banks will not be long-term survivors. Courage is doing things even when you are scared. Being brave isn't something that happens when you aren't scared anymore. Brave people don't stop hearing the whispers of fear. They hear the whispers but take action anyway!

Recently, we have seen many examples of bankers coming together to provide solutions with regard to the Coronavirus as well as challenges and issues that are facing all community banks. The California Community Banking Network ("CCBN") recently held two free pop-up calls for community banks to provide information on the Coronavirus as well as the financial impact of the virus. These calls had almost 200 in attendance for the first and 100 in attendance for the second.

These pop-up calls were free, designed basically to provide information and provide a helping hand to all banking institutions. It's only through working together and helping each other that we can show the right hero virtues and move beyond the significant challenges that face our banks, our communities and our world. This is not a time to be greedy. This is not a time to think "I." This is a time, basically, to think "we."

The following are some thoughts with regard to the four qualities of being a Hero:

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WE NEED A HERO, NOW!

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1) **Help**. Heroes help people with no strings attached. What Brown sees in this quality ties to the concept of being servant leaders. For several years we have written on the importance of community banks being servant leaders. The top exceptional banks are those who serve others and see this as a great opportunity for our banking institutions to make a difference and help. They know what the extra mile, the extra bit of works means, especially for those who touch their bank.

A hero's actions, basically, have no pretense, no conditions, no agreements, no contingencies. They truly are servants. We've seen many banks, over the last few weeks, really take an aggressive position with regard to serving their communities, getting information out to their partners, and doing whatever is needed to help everyone get through the challenges.

2) Heroes create an **Exceptional** experience for the people they serve. Brown emphasizes that heroes who create an exceptional experience are not ordinary with the occasional burst of exceptional. They do it every single time. They believe if they are going to put their name on it, it's going to be done on the level of excellence to which most people do not even aspire.

You see this on so many occasions with regard to our community banks, as well as the top exceptional banks. When they get behind something, they want to be certain they are not doing it just 100%, but 110%. They are committed to making difference. Quality of service and exceptional experience is non-negotiable. Community bankers are creating connections/relationships and not just transactions.

3) Heroes take **Responsibility** for their attitude, their actions, and results. Accountability is the key. Accountability is about self. What can we do to perform at a higher level? Whether it's a Patrick Lencioni book, looking at the legacy of the *All Blacks,* being a servant leader, or staying out of the box, it starts with basic ownership and accountability. We must take ownership for our actions and how we behave. We must be held accountable to all.

At the same time, we also need to hold others accountable for their actions. The exceptional banking institutions who are truly heroes are those who make certain that everybody who is connected with their bank is held accountable. They take ownership of their own actions, and they are committed to making a difference. If there are individuals within your bank who are not willing to take responsibility, then frankly, why are they with your bank?

4) Heroes see life through the lens of **Optimism**. Brown emphasizes that optimism is different than positive thinking. People are afraid of the idea of being optimistic because they are afraid that they will be labeled as some type of positive-thinking freak. This isn't what Brown focuses on. Brown believes an optimist encounters the same challenges, roadblocks, or obstacles and they face them head on. They don't pretend it doesn't exist. They acknowledge it as a problem. They require focus and attention to conquer. They also don't let somebody else's opinion or perspective become their own. They take ownership of their own opinions, understand what it takes to make a difference, are comfortable in their own skin, and they truly believe they have the capacity to implement change. Why shouldn't our community bankers believe this?

While there are some significant challenges facing our community banks as well as our world today, we know there are exceptional bankers out there, the true heroes who are grabbing a hold of these challenges, making a difference and leading us into a better world.

We need heroes now. Where are they? Well, for the most part, they are around you. They are your community bankers, directors, staff, various consultants and regulators. They can all be heroes. They can all make a difference. Why not take the challenge that all of us can be heroes together?

I encourage you to read *The Hero Effect*. Why not be a hero now?

Gary Steven Findley*, *Editor

TRUST IS BUILT THROUGH INTERACTIONS

Ever since I graduated from high school 20 years ago, I moved around a lot. One year in Colorado, three years in LA, two years in Charlotte, one year in St Louis, five years in Belgium, and now eight years in Denmark. As I moved around, I had to learn how to make friends and quickly connect with colleagues. And truth be told, I am not naturally gifted at doing this. I am a true introvert and trying to form relationships with strangers was not something I enjoyed.

When I look back over the years, I ended up making friends with the people closest to me, and I don't mean closest in terms of similarity or connection. I mean closest in terms of I saw them a lot. My closest friends in Charlotte were my neighbors and my classmates. My only friend in St Louis sat two desks down from me at work. This pattern continued in every place I lived. My roommates, neighbors, colleagues, and classmates were where I found friends.

Proximity and the frequency of interactions dramatically increase trust and feelings of closeness. Now this is probably not a profound revelation to anyone. We all have experienced making friends this way. But it isn't some old wives' tale we all believe. Research proves it's true. And in today's new reality of social distancing due to COVID-19, we need to understand how distance and interactions impact our relationships.

I like to read about research being done in areas of psychology, leadership, and business, and I came across this study in the book, *The Science of Likeability: 27 Studies to Master Charisma, Attract Friends, Captivate People, and Take Advantage of Human Psychology* by Patrick King. I have to give credit to King, because most research articles can be quite boring to read, and the most interesting ones are the hardest to find. But King was able to pull together some of the most interesting articles and write about them in an engaging and human manner. You don't need to be a psychologist to understand his key points.

So, I hope you like this article on how frequent interactions impact how people feel about you. I also recommend looking at my other tools and articles about working from home and virtual teams on my website: www.CavemanInASuit.com

You Have Stronger Relationships with People Who Are Physically Closer

The first study looking at how the number of interactions builds trust amongst people was published by Leon Festinger, Stanley Schachter, and Kurt Back in 1950. They examined the choice of friends and relationships within housing apartments. What they found was that relationships were often connected to how physically nearby the people lived. We now call this effect the "proximity effect." For example, people living on the second floor of a building were significantly more likely to be friends with other second floor residents, and not people living on the other floors. Even more interesting, the residents that lived near communal areas tended to have a broader range of relationships. For example, the people living near the stairwell or mailboxes on the ground floor had significantly more relationships with people on the upper floors when compared to other ground floor residents.

Festinger et al. believed that this was evidence that the foundation of friendships were small passive interactions. Very few people ever go up to someone and say, "let's be friends." For most of us, it starts with seeing each other around. Eventually, that leads to small talk and getting to know each other better. And if your interests are similar, it eventually turns into friendships. But it all starts with having small interactions.

Weradith is Why the Proximity Effect Works

At the root of the proximity effect is a phenomenon that has been studied since 1876 the "mere exposure effect." Basically, people tend to develop preferences for things merely because they are familiar with them. Through the lens of the proximity effect, friends are made with people we frequently see and are familiar with. And while that might make sense for friendships, the mere exposure effect also works on completely random things.

Robert Zajonc is by far the most well-known researcher who studied the mere exposure effect, and the majority of his studies showed just how silly the mere exposure effect can make people act. He would first show

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TRUST IS BUILT THROUGH INTERACTIONS

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participants some random images. Later in the session he would reshow some of the original images, but also add in some new images. Even though these were random images with no inherent value to the person, participants would rate the originally viewed images more positively than the new images.

The images Zajonc would use were things that often meant nothing to the participants, like polygons, Chinese characters, fictitious company logos, and made up words. But merely seeing the object once transformed it from something random with no value, into something that they liked. Think about this for a second. This would mean that if I asked you to compare two made up words, Weradith and Acaer, you would subconsciously rate Weradith more positively because you were exposed to it in the title of this section.

How to Apply the Proximity Effect While Working from Home

In an office environment, the mere exposure effect and the proximity effect occur all the time. We are constantly interacting with colleagues at their desk, bumping into them near the coffee machine, and eating lunch with them. Without even thinking about it, these constant interactions built trust and positive feelings for your colleagues. Unfortunately, we are now in an environment where physical proximity is not always possible.

If you want to build or improve a relationship with a remote colleague, focus on creating many small interactions. This does not have to seem like you are a creep or you are cyber stalking the other person. Focus on normal things. Text them or instant message them to check in. Or better yet, ask them to join you for coffee. It may sound silly, but I have known quite a few teams that have practiced “virtual coffees.” In essence, people would take 5-10 minutes to have a quick phone/video meeting to just catch up and see how the other person was doing. In this manner, they were able to replicate some of the proximity effect, even though it was by planned interactions.

I also suggest that you plan the proximity effect into your team meetings. In the transition to working remotely, many leaders will have the desire to replicate their in-person work schedule (i.e., have a weekly team meeting). But only seeing your colleagues once a week can be incredibly lonely. Instead, focus on many smaller meetings where you all use video conferencing. I also suggest you always put 5-10 minutes in every meeting to talk about non-work-related topics. In essence, you need to schedule the conversations you would normally have around the water cooler.

Customer Facing Roles Need to Leverage the Proximity Effect While Working Remotely

Customer facing roles (sales, customer service, etc.) should also use the proximity effect when building relationships with customers. Salespeople tend to know this, as they recognize that initial meetings do not often lead to a sale. They know it is the subsequent visits, when the customer has started to form a positive viewpoint of the salesperson and the products / services. So, for customer facing roles, do not sit around waiting for the customer to come to you. Even if you don’t land a sale, merely visiting the customer will significantly increase their opinion of you.

But in this new work-from-home reality, your sales and customer service roles need to be living on video chat with their customers. Now is not the time to be hiding behind systems or emails. Put a face with the name, and proactively interact with your customers. By being actively aware of the proximity effect, you can leverage these small virtual interactions to build strong relationships. As you can see, half the battle of building relationships is just showing up and interacting with the other person. So, the next time you are going to the coffee machine, pay attention to what colleagues are around, and start improving some relationships.

Cary Bailey-Findley has spent the past decade building the Human Capital within three Fortune 500 companies and was awarded the ranking of #1 development organization in the world by the Association of Talent Development. He is currently building the employee development portfolio for Unity Technologies. He holds a Master’s degree in Industrial and Organizational Psychology and a Master’s degree in Business Administration.

COMMODITY VALUATIONS & BLACK SWANS

The Findley Reports, on a regular basis, seeks articles from banking sources that are valuable to the community banking industry. This month we have an article from David Ruffin, Principal of IntelliCredit, a division of QwickRate. QwickRate is a preferred service provider for the California Community Banking Network and a leader in providing analytical tools for community banks.

How They Impact Credit Quality

As a *seasoned* credit guy who helped community bankers wean away from the "collateral lender" moniker of years past and shift their focus towards cash flow lending, there's some trepidation in writing about the first cousin of collateral, commodity valuations. So forgive the back-to-the-future moment, but credit quality is still critically impacted by a given borrowing industry's underlying and directional commodity value. For example, it was the collapse of 1-4 family residential housing values that led us into the credit crisis of the great recession. Moreover, during the same period, the credit environment in regions with stronger commodity values, such as energy, experienced far less credit stress.

Pick an industry (and its economic vulnerabilities): *agriculture* (weather/tariffs & trade); *oil & gas* (geopolitical disputes/plummeting demand); *taxis* (Uber & Lyft); even *non-profits* (unanticipated negative impact of the tax reform act de-incentivizing charitable deductions). Industries' attractiveness to bankers rises and falls based on economic forces affecting their underlying value and abilities to generate profitable revenues. This brings us to the *Black Swan*.

By definition, a Black Swan is an unexpected, but very impactfully negative event. It accelerates, exponentially, the routine economic trends and cycles alluded to above. Arguably, in the great recession, it was the collapse of the bundled securities financing the housing-related lending mania. We now have our latest version of a Black Swan: *the coronavirus pandemic*. At first glance, the service-related industries are ground zero for valuation hits. But as the crisis grows, and the economic shutdowns expand, there will be few industries left unphased. There's also the sense that this event is existential, widespread in effect, and beyond our control; but unlike before, it cannot be laid at the feet of bankers. Unlike before, our industry shouldn't expect a rush of punitive measures. That's where we are; what, as bankers, do we do about the likely growing credit risk in our portfolios?

First and foremost, we can't afford to wait to see how deep the crisis goes or to receive clarifying regulatory guidance on how to respond. A lesson learned long ago: be captain of your own fate. What this means in any crisis is: 1) understand your own position; 2) quantify it; 3) and write your own narrative—before a regulator does it for you.

Determining/Quantifying Your Credit Risk Profile

Deep dives are recommended on the following key portfolio metrics:

Concentrations/Correlations - We learned from the great recession that portfolio concentrations, like speed, can kill. Concentrations, beyond just real estate, need to be assessed by peeling the onion down to sub-sets of loan types on all matters of growth, yield, and quality. Often overlooked when thinking of concentrations is the degree the bank has correlations (or related businesses) that may become vulnerable to certain industry-specific economic blows. For example, it wasn't just the direct housing and tract development loans that ushered in so many bank failures in the last crisis; the losses were exacerbated by loans to all housing-related industries.

Industries - Using NAICS codes, bankers should quantify and prioritize their concentrated exposures to most likely impacted industries. While, again, the service industries, other than perhaps grocery stores, in the current crisis appear the most obvious, each bank has its own profile to create.

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COMMODITY VALUATIONS & BLACK SWANS

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Vintages - Another lesson of the last crisis was the risk distinctions embedded in loan vintages. Loans made in the late stages of a credit cycle are prone to be the most toxic. And given the length and benignness of the current credit cycle, including the pressures for loan growth, there is ample reason for you to begin to create vintage-specific risk profiles.

Risk Grade Migrations (within Pass) - Every credit professional knows that the real art of portfolio credit risk mitigation is the focus on credit degradation within Pass categories. Waiting until the Criticized/Classified thresholds are met is too late. Somewhat because of the structural bias of the published call report standards, bankers can be caught up in the illogical phenomenon that *all loans are good loans, until they're bad loans.*

Loan Review and Servicing - Now *is not* the time to curtail loan review due to perceived good credit, impact on efficiency ratios, or recent regulatory validations of risk grading. Now *is* the time to increase and improve periodic servicing and annual reviews based on some risk adjusted measures suitable to your bank.

<u>Adopting and Documenting Your Game Plan</u>

Finally, it's important to write out your own narrative and game plan for dealing with your bank's embedded credit risk profile. You'll need to use diagnostic tools that can *quantify* the above metrics—well beyond the bluntness of being at or near certain dollar or percentage portfolio exposures. Bank's management and board, and most assuredly the regulators, should be provided dashboards and trend analyses. But, as importantly, you must *qualitatively* interpret your own risk profile and game plan.

No one can predict accurately the ultimate level of heightened credit risk that will be created by this latest Black Swan; but no one should be complacent either in assuming this is of such magnitude that it's beyond our control. One final lesson learned in the last crisis—proven by empirical data—was that banks that were late to the game in identifying their weaknesses, *always* incurred greater losses.

David H. Ruffin, *Principal*

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IS NOW THE RIGHT TIME FOR CANNABIS BANKING?

***The Findley Reports*, on a regular basis, seeks articles from banking sources that are valuable to the community banking industry. This month we have an article from Tony Repanich of Shield Compliance related to cannabis banking. So many banks are facing the questions of whether to move into this arena or expand from their current base. This article is quite timely.**

Just a few weeks ago, our conversations with bankers about cannabis banking were somewhat predictable. Those that were willing to explore it were generally driven by a necessity to build low-cost core deposits to fund often strong loan demand or replace other sources of funding. The ability to offset costs associated with fees and bring non-interest income to the bottom line was an added benefit.

Now, as financial institutions respond to the shockwaves caused by the spread of the novel coronavirus, it hardly feels like the right time to be talking about introducing a new banking program, especially one that is high-risk.

It's clear that bankers will necessarily be internally focused for the foreseeable future as they evaluate and respond to the toll this pandemic takes on their workforce, customers, existing portfolios, and short and long-term balance sheets.

So, at a time when bankers are focusing on managing day-to-day operations, not to mention inoculating themselves against the financial, credit, operational, and reputational risks posed by the virus, is now really the right time to take on the cannabis banking opportunity?

Based on what we've seen in the market – and what we've read and heard from economists and other experts over the past few weeks – we think this global financial shock is more akin to the disruption caused by 911 then the 2008 financial crisis. The fact that it's happening at a time of record-high market volatility compounds the problem, but unlike 2008, the systemic conditions that are in play are very, very different in terms of what's creating the shock. Yes, people are frightened, and they're acting with the lion's share of fear. Still, there's some consensus that the market return will be faster, the steps to recovery will be smaller due to government intervention, and the stimulus packages that are being deployed will shorten the curve on the way down and accelerate the eventual market return.

One of the first major disruptions to emerge from this crisis relates to the battle for low-cost and low-interest deposits. With the Federal Reserve slashing interest rates to zero, financial institutions have had to shift their focus from 'how do I steal quality customers away from my competition?' to 'how do I keep and protect my best customers?' It's a total about-face for our industry and has significant implications for the way financial institutions think about their portfolios.

If the last downturn is an indicator, the pressure to grow and attract low-cost deposits will wane momentarily, but these deposits will continue to be a driver of bank profitability long-term. Increasing those deposits today will protect future profitability as the economy improves. Cannabis banking can provide a lucrative new revenue stream and the opportunity for financial institutions to grow deposits with minimal competition, at least for now.

As we've seen over the past few weeks, certain sectors of the economy, including non-traditional industries, such as legal cannabis, are uniquely immune to some of the economic issues faced by the broader market. Retail store closures and labor shortages could eventually impact the industry, but so far, cannabis sales have shown strong growth. Sales in Colorado, Washington, and California surged in early March, with year-over-year sales increases of 46%, 100%, and 159%, respectively. While some of these sales were fueled by panic buying and stockpiling, other "sin businesses," like alcohol and tobacco, offer a good comparison for how cannabis sales may fare over time. During the Great Recession, for example, alcohol sales at the wholesale level held up relatively well between December 2007 and June 2009 and increased over the longer term.

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Professional Corner

IS NOW THE RIGHT TIME FOR CANNABIS BANKING?

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Finally, as net interest margins compress, financial institutions should look to non-interest income (NII) strategies to support overall profitability. Cannabis companies, especially in California, are in dire need of quality banking solutions and are willing to pay for those services. In addition to substantially higher base account charges, often without the benefit of an earnings credit to offset those charges, there are untapped cash management fee opportunities.

While none of us has a crystal ball, all indicators point to this being a short-term crisis and not a reflection of overall market fundamentals. While bankers should be thoughtful about the risks, it may actually be the right time to begin the process of understanding how the cannabis industry works, the compliance requirements involved, the operational impacts, and how serving this industry can put the financial institution in a better position to compete for new sources of low-cost deposits when the pandemic is contained and the economy rebounds.

Tony Repanich is the President and Chief Operations Officer at Shield Compliance, a compliance management platform for cannabis banking. He has 25 years of commercial and retail banking experience.

THE GOOD, THE BAD & THE UGLY

If you're a Clint Eastwood buff, you no doubt recognize the title of this article as also being the title of one of his three, in a series, of similarly themed "spaghetti westerns." Filmed in 1966, Clint Eastwood, of course, played the Good, Lee Van Cleef played the Bad, and the Ugly was admirably played by Eli Walach. The theme song from this movie is still widely held to be one of the best movie theme songs ever.

The last few weeks were insane, chaotic, and, on occasion, somewhat terrifying, and who knows what will be going on by the time you read this article. We've witnessed some incredibly "Good" by people and, unfortunately, more than enough "Bad" and "Ugly." For purposes of this article, I'm going to try to avoid the "Bad" and "Ugly," there's more than enough of that you can read or ignore, as you best see fit.

Albeit infrequent, on occasion I've been a bit critical of various agencies, along with some of the "leaders" of those agencies. It might surprise you, but I've been consistently positive towards Jelena McWilliams, Chairwoman of the FDIC. Her previous comments and thoughts have been spot-on, and once again she shows her ability to think clearly and appropriately, particularly as it relates to the community banking world. Most recently, she wrote the Financial Accounting Standards Board, requesting that they delay the implementation of CECL and, in fact, place a moratorium on that effective date for those banks that have not yet adopted CECL. In her letter, she stated her concerns that in the current environment, CECL may strain banks' ability to lend and that "growing economic uncertainties stemming from the pandemic may make certain allowance assessment factors potentially more speculative and less reliable, at this time." She additionally requested FASB to exclude coronavirus-related modifications from being considered as a concession when determining a "TDR" classification. A great big "shout out" to Chairwoman McWilliams for her actions and thought process, and, perhaps by the time you read this article, the propeller heads at FASB might have taken some action. But, in my view, CECL is fundamentally flawed and should be trash-canned, period.

There's also a "CECL" relief bill kicking around in Congress, proposed by a group of Republican Senators. I'm not very optimistic about this bill gaining much traction, certainly not in a timely manner. Congress seems to not even be able to decide whether to adjourn or not, let alone act in a clear and thoughtful manner.

In case you missed it, before adjourning, the House Financial Services Committee was quite engaged, flogging board members, executive management, and some employees at the Big Red Stagecoach. As you are most likely aware, two of Wells Fargo's board members were scheduled to testify before this Committee. Their chairwoman, Elizabeth Duke, and board member James Quigley resigned immediately following the release of a staff report, authored by some of the majority staff. I'll express no comments or position on the findings, nor the accuracy thereof, detailed in the Report, I believe to do so would be inappropriate and not in anyone's best interest. I will, however, summarize some of the key points and findings.

The actual Report is over 100 pages, and if you're so inclined, you can read it in its entirety, on the House Financial Services Committee website. Chairwoman Waters's opening statement at Charles Scharf's March 10th appearance before the Committee started by noting that he was the third CEO to testify before the Committee in less than three and one-half years. She went on to point out that the bank that he inherited was "essentially a lawless organization that has caused widespread harm to millions of consumers throughout the nation." She detailed most of the major findings from the report, noting the Wells Fargo was still under five separate Consent Orders. The same day, she authored a letter to Attorney General Barr, stating that "her staff's investigation found that former Wells Fargo CEO Tim Sloan gave false and misleading testimony during a Committee hearing on March 12,2019" and requesting that the Department of justice "takes such action as deemed appropriate."

On a final (for now) note, on March 11th, the Chairwoman issued some "gone but not forgotten" observations, directed primarily at Ms. Duke and Mr. Quigley, stating that staff found "attitudes and failures that are dismaying." She further stated that while Ms. Duke and Mr. Quigley have resigned, "they must be held accountable for the dereliction of their duties as members of the Wells Fargo board." All I can say is, be careful out there; being a director of any organization can be extremely challenging under any circumstances.

Gary writes often about courage, integrity, and leadership, and if you're reading this, you're a leader. I recently read an article in Kevin M. LaCroix's *The D&O Diary*, titled "Reflections on the Meaning of Leadership." In that article, he talks about one of Peter Moore's book's, *Endeavour: The Ship That Changed the World*. He quotes, "A leader brings out the best of those whom he or she leads." As a community banker or director of a community bank, by my standards you're a leader. As such I'd remind you that many people are listening to your every word and closely observing your actions. Stay calm, no matter how difficult that may become; if you do, hopefully others will follow. My final request of you is please go out of your way to perform a few extra "random acts of kindness." You and others will be a lot better off for it. My hope and prayers to all, and, as always, feel free to give me a call at (602) 321-9463 or drop me a note at john@findley-reports.com.

Transactions

THE ACQUISITION OF STATE BANK CORP/STATE BANK OF ARIZONA, LAKE HAVASU CITY, ARIZONA by GLACIER BANCORP, INC./GLACIER BANK, KALISPELL, MONTANA for cash and stock, February 28, 2020.

Glacier Bancorp, Inc./Glacier Bank Kalispell, Montana ("Glacier") completed the acquisition of State Bancorp/State Bank of Arizona, Lake Havasu City, Arizona ("SBAZ") in a cash and stock transaction that, when originally announced, was valued at $135.3 million or $16.67 per SBAZ common share. Under the transaction, Glacier paid 90% of the consideration in stock and 10% in cash, with SBAZ shareholders receiving $13.7 million in cash consideration and 3,001,353 shares of Glacier common stock, representing a 3.2% pro forma ownership. When this transaction was originally announced, it had a big premium: a price to tangible book ratio of 2.12%; price to earnings of 15.6%; trailing 12-month market premium of 25.8%; and core deposit premium of 14.2%. However, at closing the price to book ratio was 1.70%; price to earnings of 16.2; and the price to deposits was 21.45.

Like many financial institutions, if shares would have been converted at the time transaction was announced, it would have looked like a much better deal than when it closed, and a much better deal than today, due to the significant drop off for financial institution stocks.

Under the transaction, SBAZ was merged with and into Glacier's existing Foothills Bank division, which moved Glacier to number 15 in deposit market share in Arizona. SBAZ was the oldest and largest community bank headquartered in state of Arizona, with 10 full-service branches and approximately $678.0 million in assets as of year-end 2019.

This was a good transaction. The management and board of SBAZ did a great job of turning this institution around from a troubled institution several years ago. Glacier has proven itself an effective acquirer in the marketplace, and while we anticipated them to look at other acquisitions, we believe all acquisitions will be on hold at this particular time, primarily due to the Coronavirus pandemic and uncertainty with regard to financial institution markets.

Glacier has seen its price drop over 25% from that at the end of February 2020, when it was in the range of approximately $40.00 per share, now down below the $30.00 per share range. This moves the transaction from a value of $135.0 million at closing to somewhere in the area of $105.0 million. It's amazing what a little time can do; however, Glacier is a strong player and should come back into the marketplace and see a lift in their shares once all this noise ceases.

Recent financial information on **State Bank of Arizona, Lake Havasu City, Arizona** is as follows:

	Total Assets ($000)	Total Deposits ($000)	Total Equity Cap. ($000)	Net Income ($000)
12/31/2019	677,589	586,835	79,999	8,198
12/31/2018	655,275	557,970	71,219	8,959
12/31/2017	620,595	549,684	65,688	6,584

Based upon consideration of approximately $125.8 million, the acquisition ratios are as follows:

1. Acquisition price as a multiple of shareholder equity – 1.70 (12/31/19).
2. Purchase price as a percentage of the deposits – 21.45% (12/31/19).
3. Purchase price times previous year's equity return – 16.2 (2019).

This is one of those transactions where you wish you would have taken as much cash as possible or would have liquidated the shares, similar to how a number of financial institution shareholders are thinking at this time. However, a good transaction for SBAZ shareholders and it's better that they are now with a much larger and solid financial institution.

DEALS IN THE MAKING

There were no "Deals In The Making" to report in the month of March 2020.

MANAGEMENT CHANGES

HomeStreet, Inc./HomeStreet Bank, Seattle, Washington accepted the resignation of Executive Vice President/CFO Mark Ruh, effective June 5, 2020. Mr. Ruh entered into an agreement with the company to ensure a smooth transition with the next CFO. HomeStreet, Inc. expects to name a new CFO before June 5, 2020 and is currently conducting a search.

Wells Fargo & Company, San Francisco, California announced that both Chairman Elizabeth Duke and Board member James Quigley resigned from the board effective March 8, 2020. Charles Noski succeeds Ms. Duke as Chairman of the Board. Mr. Noski joined Wells Fargo & Company's board in June 2019 and was the former CFO of Bank of America Corp. Both Ms. Duke and Mr. Quigley had been under a lot of pressure from the regulatory agencies based upon Wells Fargo & Company's issues over the last several years.

REGULATORY MATTERS

There were no "Regulatory Matters" to report in the month of March 2020.

OTHER MATTERS

Plumas Bancorp, Quincy, California stated that it entered into a Renewal, Extension & Modification of Loan Agreement for its Promissory Note dated October 24, 2013 payable to TIB, The Independent Bankers Bank, N.A., Texas. Among other things, the Agreement extends the maturity date of its Note to March 2, 2021 from October 1, 2020 and increases the maximum amount of the Note to $15.0 million from $5.0 million. We note that a number of bank holding companies have drawn down on lines of credit as a means of supporting their capital bases. However, most of those drawdowns were completed prior to the Federal Reserve Board of Governors significantly lowering interest rates in mid-March as we went into the Coronavirus pandemic lockdown. Plumas Bancorp was wise in pulling down the extra on its line of credit as a means of supporting its capital structure on a going-forward basis.

STATUS REPORT

LendingClub Corporation, San Francisco, California ("LendingClub") announced the execution of a Definitive Agreement to acquire Radius Bancorp/Radius Bank, Boston, Massachusetts ("Radius") in a cash and stock deal valued at $185 million. LendingClub is the largest online lending marketplace, connecting borrowers and investors. Radius is a leading online bank founded in 1987 and is based in Boston, Massachusetts with more than $1.4 billion in diversified assets. Combining Radius and LendingClub will create a digitally native marketplace bank at scale with the power to deliver an integrated customer experience enabling consumers to both pay less when borrowing and earn more when saving. This is really the first transaction by a FinTech company acquiring a banking charter, and we suspect that there will be some regulatory challenges over the next year as applications are submitted. To facilitate compliance with federal banking regulations the LendingClub Board of Directors has adopted a Temporary Bank Charter Protection Agreement, also known as a stockholder rights agreement, and approved a dividend distribution of one purchase right for each outstanding share of LendingClub stock as of March 19, 2020.

The Agreement is intended to deter stock positions in excess of certain thresholds set forth by the Federal Reserve under the Bank Holding Company Act, specifically it provides for dilution of any persons or group who acquire: (1) 25% or more equity interest in LendingClub, or (2) 7.5% or more of any class of LendingClub's voting securities. This threshold automatically increases to 10% as set forth in the Agreement. The Temporary Bank Charter Protection Agreement is effective immediately and will automatically expire on either the closing or the Radius acquisition, or after 18 months, whichever is earlier.

This is a very interesting transaction in the sense that it may set the roadmap for other FinTech entities coming into the banking environment. Definitive Agreement signed February 16, 2020. Transaction expected to be consummated after regulatory approval mid-2021.

TCF National Bank, Detroit, Michigan ("TCF") announced the signing of a purchase and assumption agreement with Alaska USA Federal Credit Union, Anchorage, Alaska ("Alaska USA"). Alaska USA will acquire TCF's Arizona operations, including seven branches and deposits of certain related assets. The transaction is expected to close in the second quarter of 2020. TCF is a $46.0 billion asset bank with top-ten deposit market share in the Mid-West, and TCF has more than 500 branches, primarily located in Michigan, Illinois and Minnesota, with additional locations in Arizona, Colorado, Ohio, South Dakota and Wisconsin. Alaska USA already has a presence in the Arizona marketplace and, with the acquisition, will increase the branch total to 15. Alaska USA has total assets over $8.3 billion. No deal terms were announced.

Pacific Premier Bancorp, Inc./Pacific Premier Bank, Irvine, California ("Pacific Premier") announced the acquisition of Opus Bank, Irvine, California ("Opus") in an all-stock transaction valued at approximately $1.0 billion or $26.82 per share, based on Pacific Premier's closing price on January 31, 2020. Under the terms of the transaction, Opus shareholders will receive 0.90 shares of Pacific Premier stock for each share of Opus stock. Pacific Premier expects the transaction to be 14% accretive EPS in 2021 with a 1.8-year earn back period and an anticipated cost savings of approximately 25%.

This takes Pacific Premier into the $20 billion size range and continues to expand Pacific Premier's footprint. Opus has 46 banking offices located in California, Washington, Oregon and Arizona. Based upon the value of $26.82 per share, the price to tangible book per share multiple is 1.384; price to 2019 earnings is 16.3; the market premium is 0.7%; and the core deposit premium is 5.2%. The transaction has a fixed exchange ratio with no caps and collars. After an initial negative reaction from Pacific Premier shareholders, the deal has now caught favor and the share value has risen since a few days after the announcement.

This is a big transaction in California, and we were wondering where Opus was going since this type of alignment with another entity was expected. When looking at where Pacific Premier is currently trading and the value offered to Opus shareholders, this is considered to be less than a book-to-book deal. This is a big one to swallow for Pacific Premier. (Definitive Agreement signed, January 31, 2020. Transaction expected to be consummated 2nd Quarter 2020.)

Bank of Southern California, N.A., San Diego, California ("BCAL") entered into a definitive agreement to acquire CalWest Bancorp/CalWest Bank, Rancho Santa Margarita, California ("CalWest") in a cash transaction valued at $32.0 million. This equates to approximately $0.43 per share, and with the transaction, BCAL will have pro forma assets of approximately $1.1 billion.

BCAL has been an effective acquirer over the last few years, taking institutions that are slightly scratched and dented, and we see CalWest as a slightly scratched and dented entity that has underperformed in the marketplace. In fact, the book value per share at the end of 2018 was at $0.22, and this is almost two times book value, which raises a serious question – why? Well part of the answer is the reversal of the tax loss which enhanced CalWest shareholder equity. In the third quarter, CalWest reversed almost $5.4 million in taxes, which increased shareholder equity at to almost $26 million. Maybe there is a silver lining to a significant negative retained earnings. BCAL has shown it's an effective acquirer, and it will likely be able to achieve the cost saves. In addition, this is an in-fill into its Southern California strategy. The acquisition ratios after considering the reversal of the tax loss look like 1.3 times book value, 23.9 times earnings, 14% of assets, 15% of deposits and a tangible book value premium to core deposit ratio of 3.1%. Pretty pricey without the tax loss reversal.

Currently, BCAL operates 11 branch locations in San Diego County, Riverside County, Orange County and Los Angeles County. CalWest is headquartered in Rancho Santa Margarita, with three office in Orange County and one office in Redlands. A nice in-fill strategy. Shareholders of CalWest who recapitalized the institution back a few years ago at $0.20 per share have seen a nice appreciation in the value. The transaction, at over 20 times 2018 earnings, is also pricey since CalWest did not pay taxes due to negative retained earnings. Maybe that is the silver lining? It will be interesting to see how the industry responds to BCAL's aggressive pricing with regard to what is delivered; however, again, BCAL has shown itself to be able to make lemonade out of lemons.

In addition, BCAL completed a private placement if $12 million of common stock at a price of $12.00 per share as a means to assist in the financing of the transaction and also for continued growth support. (Definitive Agreement signed October 21, 2019. Transaction expected to be consummated 2nd Quarter 2020.)

DE NOVO

Endeavor Bank, San Diego, California completed the sale of $7.9 million of its secondary capital offering.

CALIFORNIA COMMUNITY BANKING NETWORK

Financial Risk During Widespread Disruption: What the Board & Management Should Monitor

90-minute webinar

April 13, 2020

(recorded webinar also available)

COVID-19 is already having a huge impact on the economy. But closer to home, how is it likely to affect your bank's financial health? Join us to learn more about the impact and how to monitor key financial gauges during this epic disruption.

AFTER THIS WEBINAR YOU'LL BE ABLE TO:

- Spot weakening trends in your loan portfolio
- Understand key considerations for assessing capital adequacy through stress testing
- Assess crucial considerations for interest rate risk in a highly volatile environment
- Track key liquidity indicators
- Ask pertinent questions about re-engineering your processes and workflow for more offsite staff

WEBINAR DETAILS:

Few of us foresaw the sudden, significant impact on the financial industry that the coronavirus has brought. After many years of economic growth and stability, the impact may be significant. This webinar will address aspects of your bank that are most likely to be impacted, key indicators of your organization's health, and what to monitor to quickly identify weaknesses. You'll receive practical suggestions to keep you on top of your bank's health, which is critical for timely decision-making. **Attendance certificate provided to self-report CE credits.**

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