

NORTHWESTERN Banker Newsletter

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Improving Commercial Loan Profitability

"Banking has been hung up on the idea that it is a 'service' industry for too long. The connotation for banking as a service industry has been that it must undercharge for performing its function and apologize if profits improve."

This is the premise upon which Kenneth D. Hansen, assistant vice president, United States National Bank of Oregon in Portland, based a recent talk given to the Puget Sound Chapter of Robert Morris Associates.

A former bank auditor, Mr. Hansen is convinced that bankers "are inclined to take commercial loan profitability too much for granted."

His article is based on a talk he gave to RMA's Puget Sound Chapter. The talk, in turn, was a summary of the thesis he submitted last year to the Pacific Coast Banking School.

In giving his ideas on how banks can go about improving commercial loan profitability, Mr. Hansen starts off with a questioning look at several components of deposit account analysis: float determination, reserve requirements, earnings allowance for funds available for investment, service charges, and compensating balances.

"Deposit account analysis," he says, "should not be an exercise in futility with allocation by rationalization, but should employ cost accounting to provide the necessary expense and income information to 'tell it like it is.'"

In analyzing the deposit relationship,

Mr. Hansen chides "too many bankers accept at face value the account analysis information provided by the operations department without ever questioning the accuracy of the information."

As an example, he submits that his own observations show that the average daily float figure is closer to 1½ days than the fairly customary 1 day assessed at many banks. The additional fraction, he continues, should be assessed against the customer not absorbed by the bank as an expense that reduces profitability.

As for reserve requirements, Mr. Hansen questions deducting them from collected balances. He sees no reason why a bank should not "consider them as its own expense, figure that expense in as a cost of loanable funds and charge an appropriately higher interest rate which would be totally justified and much more acceptable to the customer."

On service charges, Mr. Hansen states that "it is this area that affords banks their greatest opportunity to improve income from improved knowledge of their costs." Failure to know their costs and to set prices that can be factually justified makes bankers easy prey for corporate treasurers with multi-bank relations, he adds. "Too frequently the banker winds up reporting his costs to such corporate treasurers."

From his look at components of deposit account analysis, Mr. Hansen next turns to a review of loan income measurement. He believes that a major share of the improvement in bank earnings will need to come



PICTURE OF THE WEEK—The concourse of the First National Bank of Minneapolis is currently filled with a wide variety of trees . . . as a part of the annual Green Giant promotion at the bank. Here, Kathy Heichel, a secretary in the marketing services department, holds a Norfolk Island Pine. It's one of a dozen Green Giant items being given away to those who qualify for the offer. One of eleven different trees can be selected at any of the five Green Giant Home and Garden Centers in the Twin Cities. Or, customers can choose a terrarium, which is available right at the bank.

from sources other than interest, such as fees and loan handling charges.

Interest, he says, is becoming a victim of continued and increasing pressures as more loanable funds are purchased and competition from other financial intermediaries increases.

Mr. Hansen next turns to a discussion of risk as a factor in pricing. "Loan loss experience and expectancy by categories of loans," he says, "should be considered in analyzing risk and setting interest rates."

As for assigning a percentage of capital to loans according to risk analysis, Mr.

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IOWA NEWS

ALBIA: The correct telephone number for The Peoples National Bank is 515/932-2124. It was printed incorrectly in the Iowa Bank Directory.

BENNETT: Dale C. Froehlich has been named cashier of the Bennett State Bank. He was formerly with the Farmers Savings Bank, Princeton.

CLARION: The Wright County State Bank has changed its name to Brenton Bank and Trust Company, according to Robert D. McKee, bank president.

KEOKUK: An application by the Security State Bank to establish a bank office in the Keosippi Plaza Shopping Center has been approved.

LIVERMORE: The correct phone number for the Livermore State Bank is 515/379-1435. Subscribers to the Iowa Bank Directory should note this correction.

MANCHESTER: Following is a correct list of officers for the First State Bank: W. K. Wiewel, president and chairman; L. W. Justice, executive vice president; R. W. Teske, vice president, Mary R. Duggan, cashier; Betty Lois Koelker and Joseph Wiewel, assistant cashiers.

MUSCATINE: Robert Solheim has been named vice president and trust officer for the First National Bank.

OELWEIN: Cliff Avery has been named vice president of the First National Bank. He joined the bank in 1947.

SIOUX CITY: William C. Orr, assistant auditor at First National Bank, has been elected president of the Sioux City chapter of the American Institute of Banking.

NEBRASKA NEWS

BEATRICE: W. W. Cook, Jr., president, The Beatrice National Bank and Trust Company, has announced the following staff changes in his bank and affiliate banks: D. E. Osmera, formerly president of the Pickrell State Bank, has been elected executive vice president of the Wymore National Bank, succeeding D. Dean Kecheley who accepted a position with a Des Moines, Ia., bank. Steven G. Latham was elected vice president of the Pickrell State Bank. He had been assistant vice president, commercial lending, Beatrice National. John C. Rypma, formerly assistant vice president, instalment loans, Beatrice National, will now be assistant vice president, commercial loans.

CRETE: Funeral services were held recently for Frank E. Krivohlavek, assistant cashier, City National Bank. Mr. Krivohlavek joined the bank in 1966 as agriculture representative and was promoted in 1967.

NORFOLK: The Bank of Norfolk has filed an application for a detached auxiliary teller office at 920 South 13th Street in Norfolk. A hearing has been set for 9:30 a.m., July 10, Department of Banking, Lincoln.

OMAHA: The Omaha State Bank has moved into permanent quarters at 12100 West Center Road near the southwest corner of the BelAir Shopping Plaza, accor-

ding to Gene Zaloudek, bank president. A grand opening is planned later this month.

OMAHA: A hearing has been set for July 5, at 9:30 a.m., Department of Banking, Lincoln, on the Douglas County Bank of Omaha's application for a detached auxiliary teller office at the northeast corner of the intersection of 108th Street and Mockingbird in Omaha.

OMAHA: Darryl D. Hansen has been elected commercial loan officer of the Center Bank.

ILLINOIS NEWS

BELLWOOD: Lawrence P. Buckley has been named senior vice president of the Bank of Bellwood.

CHICAGO: Don R. Conlan, economist with Capital Research Co. and Dean Witter & Co., will address a dinner meeting of the Chicago chapter of the Financial Executives Institute in the First National Bank of Chicago, May 31.

CHICAGO: American National Bank & Trust Company has appointed Thomas R. H. Ransom and Howard E. Lovely vice presidents and Andrew B. Albert, Robert E. Fulton, Sr., and Jerome R. Thomas second vice presidents.


EAST MOLINE: The board of directors of the State Bank of East Moline recently elected Jeffrey P. Roelens vice president, cashier and secretary. He joined the bank seven years ago, and was promoted from assistant vice president, operations. Dixie King was elected assistant cashier, operations.

PALOS HEIGHTS: An application for a permit to organize The Union Bank of Palos Heights has been filed. The bank would have total capitalization of \$1 million. Applicants are: Harold F. McGrath and Calvin K. Bouma, Palos Heights; Robert B. Rew, Flossmoor; David L. Rauen, Hickory Hills; Alex J. Buvidas, Chicago, and Terrence O'Brien, Hazel Crest.

MINNESOTA NEWS

AUSTIN: The First National Bank has announced the following staff changes: S. W. Schneberger, formerly installment loan officer, has accepted a position as manager,


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installment loan department at First National, Blue Earth. George S. Adams III has assumed duties in the audit department. Michael Chapman has joined the bank as an installment loan officer.

DULUTH: Eugene R. Lambert, publisher of the Duluth Herald and News-Tribune, has been elected to the board of the First American National Bank, according to Chester C. Lind, bank president. Promotions announced are: Ralph J. Mrak from assistant vice president, systems planning department, to vice president; Joel W. Schmidt from operations officer and cashier to vice president, and Arthur W. Danielson from assistant vice president to cashier.

EAGAN: JoAnn E. Class was promoted to cashier at the Valley National Bank.

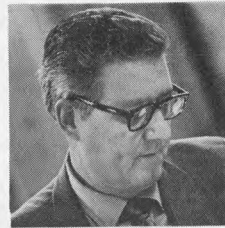
FAIRMONT: Osmer M. Fowler, cashier of the Martin County National Bank, died recently after a lingering illness. Mr. Fowler was associated with the bank for 47 years, starting as a bookkeeper, teller, assistant cashier and then cashier.

GRANITE FALLS: Marshall Diebold has purchased the Blomquist family stock in the Granite Falls Bank. Mr. Diebold is vice president and director of Northrup, King and Company. F. L. Wilson, president, Ernest Rottunda and Therol Velde, along with Mr. Diebold and his son, James, will constitute the new board of directors.

HOLLANDALE: John R. Buley was promoted to president and cashier of the Produce State Bank, filling the vacancy created by the death of Cornelius Kraay, president and director for 30 years. John Van Erkel was elected to the board to fill that vacancy.

HUTCHINSON: Thomas F. O'Connell has been named vice president in charge of trust services at Citizens Bank & Trust Co. He was formerly a bank examiner for the Minneapolis region of the FDIC.

MINNEAPOLIS: David A. Heider was elected president of Gambles Continental



Bob Bueneke

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ROCHESTER: Rochester State Bank has announced three promotions: John Huemoeller from vice president to senior vice president, Cedric Linville from assistant vice president to vice president, and W. Wayne Ellison from an assistant vice president to cashier.

RUSHFORD: Albert C. Spande has been elected agricultural representative of the First National Bank.

SAINT PAUL: Ronald Brue, White Bear Lake, has been elected assistant vice president of First Bank System, Inc.

SAINT PAUL: John A. Ritt, Afton, was elected president of Midway National Bank.

WORTHINGTON: Howard W. Meyer has been promoted to vice president of the State Bank of Worthington.

COLORADO NEWS

DENVER: The following staff changes have been announced by Don Hoffman, president of The Central Bank and Trust Company: Allen K. Thomas, former loan officer in the petroleum department, commercial loan division, Chase Manhattan Bank, New York, joins Central as vice president. Charles J. Wolf has been elected a loan officer in the commercial loan division; Donald O. Daniels has been named loan and discount officer, and Raymond R. DeMoro has been named an international operations officer.

STERLING: The boards of directors of The First National Bancorporation, Inc., and The Security State Bank of Sterling have agreed on a revised exchange ratio under which Banco would acquire the Sterling bank. The revised ratio would be 21 shares of Bancorporation common stock for each share of Security State common.

Completion of the acquisition is still enjoined as a result of an anti-trust suit pending in the United States District Court for the District of Colorado.

SOUTH DAKOTA NEWS

SIOUX FALLS: Donald F. Bertsch has been elected vice president and cashier of the National Bank of South Dakota, according to Don W. Westbee, chairman. He was formerly controller and will succeed Robert M. Haugen who has assumed a position in the bank's western division headquarters in Rapid City.

NORTH DAKOTA NEWS

FARGO: The Merchants National Bank & Trust Co. has added a marketing officer to its official staff, according to A. K. Simpson, president. Russell H. Slotten has joined the bank as assistant vice president to handle the new position. He formerly was director of public affairs for the Dayton-Hudson Corporation in Minneapolis.



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LOAN PROFITABILITY . . .

(Continued from Page 1)

Hansen subscribes to using the same percentage on all loans.

Finally, he looks at the cost of loanable funds. He is a proponent of the marginal cost of money approach which holds, basically, that when a new loan is made, the needed funds are seldom raised at the average cost of the deposit mix but rather purchased at the going rate in the market place. He advocates using the CD rate as a key in determining the cost.

Thus having given his analysis of realistic accounting for income and expense, Mr. Hansen concludes with a discussion of a method he has devised of measuring profitability.

A form he has created is included in the article. It allows a relatively simple comparison of income to expense on any particular loan to arrive at its net profit before taxes. This net profit figure is then measured against the bank's desired goal—predetermined by management for that loan—to arrive at the profitability index. It is the index figure, of course, that shows whether or not the loan is providing an adequate return for the bank.

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POSITION WANTED

Young man, age 25, desires banking position in agriculture credit or ag management. B.S. degree in agricultural business and farm management and M.S. degree in agriculture economics from Iowa State University. Prefers Iowa location. Available in July, 1973, Write Box OWS, NORTHWESTERN BANKER, 306 - 15th Street, Des Moines, Iowa 50309.

POSITION AVAILABLE

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FOR SALE

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