Combatting Consolidation in the United States Banking Industry: An Analysis of Performance and Strategy of First National Bank of Clarksdale

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COMBATTING CONSOLIDATION IN THE UNITED STATES BANKING INDUSTRY: AN ANALYSIS OF PERFORMANCE AND STRATEGY OF FIRST NATIONAL BANK OF CLARKSDALE

by
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ABSTRACT

LYDIA KATE JOHNSEY: Combatting Consolidation in the US Banking Industry: An Analysis of Performance and Strategy of First National Bank of Clarksdale
(under the direction of Bonnie VanNess)

This thesis is based on a submission with group members in the 2023 Case Study Competition for the Conference of State Bank Supervisors. This thesis includes additional background information not included in the original competition paper in order to clarify the competition standards and goal of the paper. This thesis evaluates First National Bank of Clarksdale with respect to two areas: financial analysis, which evaluates earnings performance, loan portfolio composition, asset growth, capital levels, and liquidity of the bank; and strategy, which includes staffing, succession, training, and technology strategies instituted by bank management. Data from the bank's Uniform Bank Performance Report and the Federal Deposit Insurance Corporation 10-K filing, together with the strategic management planning and storytelling outlined in interviews with bank management, offer robust insight to the effectiveness of First National Bank of Clarksdale in warding off takeover and preserving its community bank business model. Collectively, the quantitative and qualitative data gathered suggest that FNB Clarksdale is at risk for takeover if it continues to underperform its peers.

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INTRODUCTION

The purpose of this paper is to draft a competitive submission for the 2023 Community Bank Case Study Competition offered by the Conference of State Bank Supervisors (CSBS) to undergraduate students in the United States. The purpose of the case study is to create partnerships between academics and community bankers, simultaneously granting students a real-world research opportunity and giving community bankers the chance to tell their stories. The official topic given for the competition is attached in the appendices; however, to clarify the structure of the paper, it is important to note that the topic contains three parts. The first part requires a financial analysis of the institution, with respect to five elements: earnings performance, loan portfolio composition, asset growth, capital levels, and liquidity. The second part, listed as "staffing," and third part, listed as "training and technology," each give six guiding questions, requesting that the team ask the most pertinent questions to the institution, giving discretion with respect to the content and structure of the latter two parts. Upon reading these guiding questions, we note a pattern for the second and third sections; some questions were geared towards strategy, others asking for stories of the institution. Thus, we structure the paper as follows: *Section I: Financial Analysis*, with five subsections corresponding to the five required elements, *Section II: Staffing and Succession*, with four subsections corresponding to strategy and storytelling of the two titled elements, and *Section III: Training and Technology*, with four parallel subsections to mirror those of Section II. The original paper submitted for the competition has a 25-page limit which guides original formatting decisions; the addition of this introduction, the list of figures and tables, the appendices, and new positioning of tables and graphs have since been implemented to make the paper more cohesive.

EXECUTIVE SUMMARY

Consolidation of the United States banking industry has placed new threats on the future of community banking, especially in rural communities. These threats are likely to increase for the foreseeable future. In this study, we analyze the financial performance and corporate strategies of First National Bank of Clarksdale, Mississippi (henceforth, FNB Clarksdale). In conducting this analysis, we hope to better understand how FNB Clarksdale prepares to sustain itself against stringent challenges faced in staffing, succession, training, and technology in its fast-changing industry.

FNB Clarksdale is located in the city of Clarksdale in Coahoma County, Mississippi, of the rural Mississippi Delta region, which is renowned for its fertile farmland. Despite its success in the agriculture industry, the Mississippi Delta region is, "among the poorest, if not the poorest, section of the nation based on virtually every socioeconomic measurement." With respect to demographics, the percentage of persons in Coahoma County living below the poverty line is more than four times the national rate for 2021; the percentage of persons unemployed is more than 1.5 times the national rate for December 2022; and the county is 77.7% African American, compared with a 13.6% national African American population. We provide these statistics to show that the community to which FNB Clarksdale provides financial services is marked by significant socioeconomic differences from the rest of the nation. Additionally, Coahoma County experienced a 20.3% decline in population from 2010 to 2021.

When FNB Clarksdale management sought to diversify in the early 2000's, the bank established an additional branch in Oxford, Mississippi, approximately sixty miles east of its main branch. This new branch was established under a different name, Bank of Oxford. Oxford,

Mississippi, is home to the state's flagship university and is located in Lafayette County, which has a commercialized market. Lafayette County boasts a much lower poverty rate for 2021, at nearly half that of Coahoma County; the percentage of persons unemployed is not only half that of Coahoma County, but also 1.1% below the national rate for December 2022. The county is 71.9% white and experienced a 17.9% growth in population from 2010 to 2021. Essentially, Lafayette County contrasts Coahoma County in industry, socioeconomic factors, demographics, and population growth rate, which made the decision to enter this market an obvious choice to bank management for diversification purposes.

With an asset size of $407 million and a presence in its communities for almost sixty years, FNB Clarksdale has onboarded and developed talented individuals while consistently implementing changes in technology in order to build and strengthen customer relationships. The bank seeks to maintain its current business strategies and pursue growth that comes from the pursuit of its relationship-based business model.

In order to assess the sustainability of FNB Clarksdale, we conducted both a financial and strategy analysis. In *Section I: Financial Analysis*, we examined the financial performance of the bank by five means: earnings performance, loan portfolio composition, asset growth, capital levels, and liquidity. We perused the bank's FDIC 10-K filings and the Uniform Bank Performance Report (UBPR) to gather raw data. We constructed a peer group of comparable banks to perform a benchmark analysis. We included all community banks in the state of Mississippi in the peer group, as opposed to only concentrating on those of the Mississippi Delta region, in order to account for the diversity in customer base that comes with having branches inside and outside of the Delta. We computed peer comparison values by averaging each relevant UBPR data point for the comparable banks. We organized the data into graphs and tables to illustrate yearly changes and simplify our analyses. Lastly, we interviewed top executives to probe into factors explaining changes in financial performance in order to gain a more thorough understanding of the driving influences behind the data. In *Section II: Staffing and Succession*, we discussed FNB Clarksdale's strategies for staffing and succession planning from the previous ten years. We derived information from the bank's annual report and provided insight from interviews with bank management. In *Section III: Training and Technology*, we discussed FNB Clarksdale's strategies for training new hires and developing current staff, including the implementation of any recent changes in technology, using insight provided by bank executives.

We found in *Section I: Financial Analysis* that earnings performance for FNB Clarksdale was inconsistent, improving in some years and declining in others; in addition, the bank slightly underperformed its peers each year. Loan Portfolio Composition for FNB Clarksdale held a significant and growing portion of agriculture loans, which distinguished the bank from its peers. Asset Growth for the bank has been increasing steadily year-over-year. Capital Levels for FNB Clarksdale met both Basel 2.5 Accord and Basel III Accord minimum requirements. Lastly, Liquidity was not a problem for the bank. We found in *Section II: Staffing and Succession* that FNB Clarksdale recruited, hired, and developed new employees either from the communities it served, from state universities, or within the company; the bank looked to promote from within when selecting a successor, and the bank did not see much turnover in its middle, senior, or executive level positions. We found in *Section III: Training and Technology* that FNB Clarksdale cross-trained employees to be competent in multiple job functions and offered opportunities for further education to top-performing employees. With respect to technology, we found that the bank had a reactive response to consumer demand in implementing new technologies made possible by its close relationships with customers.

The ability of FNB Clarksdale to ward off takeovers can be perceived through a close analysis of its financial performance, recruiting and sustenance strategies, and ability to keep track with the implementation of up-to-date technologies. This analysis is beneficial to financial institutions, investors, and regulators.

SECTION I: FINANCIAL ANALYSIS

Section I.1: Financial Analysis Overview

We performed a five-year time-series and benchmark financial analysis of FNB Clarksdale, in accordance with the CSBS Part I guidelines cited in *Appendix A*. We developed a holistic understanding of its financial performance from 2018 to 2022 by gathering quantitative data from the UBPR and FDIC 10-K filings and qualitative data from interviews with executive management. We presented figures as visual representations of our quantitative data. We compared the performance of FNB Clarksdale to the average of a peer group of community banks located in Mississippi. We selected this peer group based on FDIC Mississippi community bank classification standards. We created a peer group encompassing all community banks located in Mississippi, rather than a narrower group of community banks located in the Mississippi Delta region, to account for the performance effects of the branch Bank of Oxford on the financial institution. Our findings suggested that FNB Clarksdale is well capitalized and liquid enough to exploit further profitability opportunities by issuing more loans and increasing the loans-to-deposits ratio.

Section I.2: Earnings Performance

Due to the consolidation of the United States banking industry, the number of small banks in America has fallen and the current need to assess the profitability of a community bank has become crucial in determining whether or not the bank would be a target for takeover. To assess the earnings performance of FNB Clarksdale, we obtained the return on equity, return on assets, net interest margin, and yield on returning assets from FDIC 10-K filings. At first glance, we observed that FNB Clarksdale has experienced dynamic changes in its earnings performance for the past five years, as seen in Figure A1 in *Appendix A*.

In our analysis, it was noteworthy that FNB Clarksdale was underperforming before COVID-19; as seen in Figure A1, from 2018 to 2019, ROE for the bank fell from 9.46% to 2.90% while the peer group remained relatively stable at respective levels of 10.34% and 10.50%. This decline in earnings performance was the result of a one-time settlement in the Arthur Lamar Adams ponzi scheme, the largest ponzi scheme in Mississippi history, in which the bank experienced a loss. This ponzi scheme had boasted returns of 13% from a timber broker enterprise facade that defrauded approximately 300 investors of over $100 million. The bank took a hit, and for that reason, Figure A1 displays significantly larger gaps between the performance of the bank and the performance of the peer group in 2019.

On the positive end, 2020 was a better year for earnings performance, with ROE increasing to 8.65% from 2.09% in 2019. The bank decided to faithfully serve the markets to which it had successfully been making loans before the ponzi scheme. Earnings continued to grow, and 2022 was the bank's best-performing year. The bank still trailed behind the peer group, and according to management, this trailing was largely due to low interest rates over the past five years squeezing profit margins on loans and growing competition in both Clarksdale and Oxford markets increasing pressure on yields.

Being a community bank, FNB Clarksdale did not enjoy the same scale advantages as larger banks, which made it more difficult to offer competitive rates, hurting profit margins. However, FNB Clarksdale was well capitalized, and the bank currently has the capacity to make more loans to drive profitability. Additionally, interest rates rose in 2022, and because agriculture loans reprice every year, FNB Clarksdale has reaped the benefits of this rising rate environment.

By capitalizing on the opportunity to derive earnings from higher-rate loans and maintaining a strong emphasis on its relationships with customers, FNB Clarksdale can maximize the interest spread.

Section I.3: Loan Portfolio Composition

FNB Clarksdale distinguishes itself from other community banks in Mississippi by making large amounts of agricultural loans. This distinction is not surprising, considering the bank's location in the Mississippi Delta region. The bank has diversified its loan portfolio; a few notable changes, as seen in Figure A2, were the increase in the percentage of the portfolio given to agricultural loans, which were up 10.67% over the five-year period, and the steady decrease in the portion given to real estate (RE) and commercial and industrial (C&I) loans, which were down as a portion of the asset portfolio by 8.58% and 1.46%, respectively.

The growth in agricultural loans stems from the strategic addition of new customers in Clarksdale, notably in 2022. Further, because of the chance to capitalize on the changing rate environment, it made sense for the bank to grow agriculture loans with the expectation that they will reprice at a higher rate.

The strategy behind opening the Bank of Oxford branch in the early 2000’s was to diversify the bank’s loan portfolio. While the market in Clarksdale is heavily concentrated in agriculture, that of Oxford is more saturated with commercial RE and C&I loans. The addition of these loans stabilizes the rate environment and mitigates interest rate risk amidst the annual repricing of the agricultural loans. The general decline over time in RE and C&I loans is derived from their low profitability due to increased competition and the bank’s strategic growth of its share of agriculture loans and commitment to serving customers in the Mississippi Delta.

Section I.4: Asset Growth

Asset growth for FNB Clarksdale has been stable for the past five years with the exception of a slight decrease during 2019 resulting from the ponzi scheme loss, shown in Figure A3. The bank experienced an increase in deposits over the five year period, the effects of which include an increase in loans originated and total asset growth of $44.5 million. During 2020, the bank held a higher amount of cash on hand than previous years due to the influx of deposits from the implementation of the Paycheck Protection Program (PPP) from the United States Small Business Administration, which allowed community banks to advocate for their customers and apply for loan forgiveness for qualifying small business owners. These assets were held on the books, meaning they were not used to issue new loans, for up to two years due to the fact that the PPP application process had two rounds, one in April 2020 and another in January 2021.

As the immediate COVID-19 pandemic uncertainties have subsided and the Federal Reserve has raised interest rates, American banks are now required to make new investments to keep the net interest margin as high as possible. FNB Clarksdale management attributes its growth in assets during the period to its deepening relationships with the communities it serves at both locations.

Section I.5: Capital Levels

Most banks measured capital levels in accordance with the Basel II.5 Accord, which set the minimum amount of liquid capital to be kept on hand for financial institutions, until the implementation of the Basel III Accord in 2023. These accords apply to two tiers of two ratios that gauge capital levels. The tiers are Tier 1, which includes the core capital of owners' equity and retained earnings that are disclosed in financial statements, and Tier 2, which contains any undisclosed funds in addition to the capital in Tier 1. The two benchmarked ratios are the leverage ratio and the capital ratio.

However, in 2018, community banks were given clearance to measure capital levels by a new Community Bank Leverage Ratio (CBLR), upon the passing of the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018. This legislation reduced the burden of calculating and reporting risk-based ratios for banks with asset sizes under $10 billion. Therefore, in calculating capital levels of FNB Clarksdale, we benchmarked the bank's simple leverage ratio with the CBLR minimum of 9%. FNB Clarksdale well surpassed these guidelines each year, as seen in Figure A4, signifying that the bank was well capitalized; thus, if FNB Clarksdale were to face another liquidity issue, as seen in the circumstances following the Arthur Lamar Adams ponzi scheme, the sufficient amount of capital held would provide a buffer to allow the bank to remain solvent. Bank management is satisfied with the bank's current capital ratios and does not perceive a need to raise capital since exponential growth in the coming five years is not anticipated.

Section I.6: Liquidity

We measured liquidity of FNB Clarksdale by the loans-to-deposits ratio (LDR). Because FNB Clarksdale is a community bank, one with such a small asset size in a rural market, deposits are small and typically insured. Therefore, core deposit levels are nearly always the same as total deposits. Thus, we measured LDR based on total deposits, rather than core deposits, to make up for the lack of core deposit data for 2018. As seen in Table A1, our findings show that, for the past five years, the bank did not have an LDR greater than 67.04% or lower than 57.82%. These values signify that the bank loaned out no more than 67 cents and no less than 58 cents of every dollar deposited. Thus, the bank had at least 33% of deposits on hand every year, making it highly liquid. Further, as also seen in Table A1, the bank remained at higher levels of liquidity than the peer group for every year other than 2022.

Because of its low LDR and the low interest rates prior to the pandemic, FNB Clarksdale did not consider itself exposed to great amounts of liquidity risk for 2018 and 2019. Several COVID-19 federal assistance programs for small business owners brought in a 15.25% surge in core deposits in 2020, strengthening management's confidence in the bank's liquidity; among these were the aforementioned PPP, the Economic Injury Disaster Loan (EIDL), and the Economic Retention Credit (ERC). This upward trend in deposits and liquidity confidence continued for an additional 4.13% increase in core deposits in 2021. FNB Clarksdale held the deposits as cash for 2020 and 2021. Because consumer spending was down during the pandemic, the bank did not experience much loan growth. The increase in deposits without an increase in loans continued to cut the LDR and drive liquidity, bringing the bank to its five-year low for its LDR in 2021.

Yet, in 2022, the FNB Clarksdale had a decrease in core deposits of 4.04% and an increase in loans of 10.81%. Thus, the LDR increased, again due to the issuance of new agricultural loans as mentioned in Section I.3, bringing the bank to near-pre-pandemic levels of liquidity. The increase in agricultural loans was strategic in the sense that it brought in revenue despite the effects of the pandemic on consumer spending and made excellent use of the surge in deposits.

Looking forward, FNB Clarksdale is astute with respect to liquidity risks. The bank recognizes the importance of paying competitive interest rates on interest-bearing accounts. Although the bank has a historically loyal customer base, FNB Clarksdale risks the loss of key depositors and would suffer a hit to its liquidity consistency if it fails to compete well in the years to come. The bank plans to mitigate this risk by offering competitive rates and deepening relationships with its customers. It has the potential to compete with respect to interest rates by using the increased income from agriculture loans repricing annually at higher rates to pay more competitive rates to its depositors.

Section I.7: Financial Analysis Summary

Upon analysis of FDIC 10-K reports and UBPR data, we noted that FNB Clarksdale was underperforming compared to other community banks in Mississippi but has beaten its previous year's performance for the past three years. We also observed that the loan portfolio of FNB Clarksdale was different from that of the peer group, consisting of a significant portion of agriculture loans largely due to the fact that the bank served the geographical area of the Mississippi Delta. Further, we noted that asset growth for the bank was slow compared to the peer group, though the growth was stable. Additionally, we found that FNB Clarksdale is highly liquid, noting that although the bank has historically held more capital than is required by the Basel II.5 Accord and is already above the Basel III Accord requirements to be implemented in 2023, it is no longer subject to those measurements but rests well above the CBLR requirement. Ultimately, we conclude that FNB Clarksdale is not under financial stress but must improve performance to maximize profits; we recommend continuing to capitalize on the high-rate environment with the strategic growth of repricing agriculture loans in Clarksdale and those of real estate in the Oxford market to push the LDR as high as the bank is comfortable in order to capitalize on the profitability potential of some of the bank's core deposits.

SECTION II: STAFFING AND SUCCESSION

Section II.1: Staffing and Succession Overview

Here, we examined the managerial strategies of FNB Clarksdale with respect to staffing and succession planning. We considered each of the questions proposed by Part II of the CSBS competition guidelines in *Appendix B*. We observed that several of the questions pertained to a staffing or succession strategy of the bank while other questions inquired about specific accounts of a time when those strategies had been implemented. Thus, we divided this section into four subsections to display the strategies and stories of FNB Clarksdale with respect to staffing and storytelling. We conducted interviews with bank executives guided by our findings from Section I to probe its process for procuring talent to fill staffing needs and to protect the bank in sustaining the loss of such talent. We inquired about current and expected challenges faced by the bank in these two realms. Lastly, we illustrated the implementation of these strategies by exploring stories of bank successes and failures in these areas. In conducting this examination, we aimed to assess the effectiveness of FNB Clarksdale in closing the talent gap and warding off the threat of being acquired by a regional or national bank with access to a larger talent pool.

Section II.2: Staffing Strategy

The staffing strategy of FNB Clarksdale includes recruitment and development of hardworking and talented individuals, maximization of the efficiency of its staff in cross-training employees, and use of this reduction in cost from increased efficiency in offering excellent benefits and competitive pay. The strategy has not changed much over time, is essentially the same at both FNB Clarksdale and Bank of Oxford, and has served the bank well.

Specifically, in recruiting fresh talent, FNB Clarksdale maintains a close relationship with key faculty of the Schools of Business at state universities for recent graduates. Additionally, the bank looks to open jobs, when possible, to the communities it serves and to develop Clarksdale or Oxford locals into prepared employees, ready to serve the bank and the community. Lastly, the bank perceives new openings as opportunities to promote and train from within. FNB Clarksdale will cross train employees in different areas to assist with new responsibilities the bank may need covered.

FNB Clarksdale prefers to have fewer employees with greater job responsibilities. In cross training employees, FNB Clarksdale cuts costs by avoiding new hires that would reduce the efficiency of the bank and uses these savings to offer its employees greater benefits. Primarily, employees are compensated financially for their willingness to wear multiple hats. In the eyes of management, a greater number of job responsibilities warrants a greater salary. FNB Clarksdale boasts that all 49.5 bank employees at every level are amongst the highest paid for their respective positions at other banks in Mississippi. Along with competitive pay, FNB Clarksdale allows employees to prioritize family and personal life with a flexible schedule. Because employees wear multiple hats, the bank staff can work as a team to pick up the responsibilities of anyone who needs to attend a familial obligation. FNB Clarksdale claims a "family-first" environment for its staff, allowing employees to enjoy more of the moments that cannot be lived again. These benefits make FNB Clarksdale a desirable place to work.

The biggest staffing challenge faced by FNB Clarksdale is within its Clarksdale talent pool for potential employees. Because the population in Coahoma County has been steadily declining, the bank finds it increasingly difficult to find people with potential to be successful employees and even more challenging to recruit qualified individuals from outside the job market into a dying community. However, the opposite is true for the branch Bank of Oxford. The Lafayette County population is growing and Oxford remains a desirable place to live and work in Mississippi. Yet, with the attractiveness of the community comes increased competition in the job market, which is another staffing challenge that bank management recognizes for its Oxford branch.

Section II.3: Staffing Storytelling

An exemplary story of the staffing strategy of FNB Clarksdale is the fulfillment of the role of Senior Vice President (SVP) in 2022. The SVP was originally hired in 2012, when he was referred to the bank by the Dean of the School of Business Administration at the University of Mississippi. For most of his time at the bank until 2016, he was thoroughly cross-trained in different bank departments. He began serving the bank as a teller, customer service representative, and loan assistant, working in each of those positions simultaneously. Additionally, he took all available opportunities to inform himself with respect to debit cards, ATMs, information technology, and credit underwriting. In 2016, he no longer served as an assistant, but rather began to build his own loan portfolio. In February of 2017, he was promoted to Assistant Vice President, then again to Vice President of Commercial Lending in 2018, where he spent the next several years building a customer base and increasing his loan portfolio. In the meantime, he attended the Graduate School of Banking at Louisiana State University, and finished the program in 2023, just after his 2022 promotion to SVP. This case is exemplary of the staffing strategy of FNB Clarksdale because it is not distinct from many of the stories of the current members of executive and senior management. Many of these key leaders of the bank were initially hired many years before, cross-trained in multiple disciplines of the bank, and promoted many times before arriving to upper management positions.

Section II.4: Succession Strategy

The official succession plan for FNB Clarksdale is kept at the office of the attorney, as is required of banks in the United States. However, bank management notes several key factors in developing a proper strategy for times of succession. First, when considering a candidate, FNB Clarksdale accounts for the overall relationship with the community as well as understanding of bank operations and strategy of the potential successor. Employees at the executive and senior levels must work closely with one another when making decisions and communicate effectively. To avoid disruptions to bank operations, FNB Clarksdale seeks to appoint a successor who works well and communicates effectively with superiors and colleagues. The bank has been fortunate to see little turnover in upper-level positions; however, when the need for a managerial successor arises, FNB Clarksdale seeks to promote from within. This succession strategy is a means of dealing with the staffing challenges of the bank; since the bank is expected to have an increasingly difficult time recruiting outside expertise to a diminishing area, it begins developing managerial talent from the point of hire.

Section II.5: Succession Storytelling

FNB Clarksdale has seen a few retirements of senior-level management in the past ten years. Specifically, two Senior Vice President (SVP) positions have seen three exits, one with two exits in 2013 and 2018, and the other with one exit in 2022. Both were filled with successors in 2018 and 2022 respectively. The valuable SVP positions manage a portion of the portfolio and maintain the relationships with those customers. Thus, when choosing a successor, the bank looked within. Fortunately, for the way the bank cross-trains employees, the candidates that filled these key management positions already had relationships with the customers and were familiar with the loans in the portfolios. Further, another succession opportunity occurred when the Chief Operating Officer (COO) of FNB Clarksdale retired in 2013 and was succeeded in 2014. As in the previous case with the SVPs, the bank looked to fill the COO position from within the bank. The bank promoted its former Executive Vice President to the COO position.

Section II.6: Staffing and Succession Summary

In this section, we find that the staffing strategies of FNB Clarksdale encompass the recruitment and development of individuals, the cross-training of employees for improvement of efficiency, and the offering of competitive benefits for retention. We find that the succession strategy of FNB Clarksdale is nourished by its staffing strategy in the sense that over time, the bank has developed its employees into a pool of potential management successors that have been growing in relationship with the community and understanding of bank operations since first hired. Thus, when the bank is looking for a successor, we find that it looks to appoint from within.

Additionally, in this section, we discuss the stories of the appointment of the current Senior Vice President of the bank and the succession of the most recent Chief Operating Officer. We find that these stories exemplify the high value that bank management places on the role of customer relationships and understanding of bank operations. Ultimately, we conclude that these strategies serve the bank well in warding off potential consolidation efforts, like acquisition attempts from larger banks, by distinguishing its small, hometown feel from the traditionally bigger, unfamiliar feel of larger banks.

SECTION III: TRAINING AND TECHNOLOGY

Section III.1: Training and Technology Overview

Here, we examined the managerial strategies of FNB Clarksdale with respect to training and technology. We looked through each of the questions proposed by Part III of the CSBS competition guidelines in *Appendix B*. We noted that several of the questions pertained to a training or technology strategy of the bank while other questions inquired about specific accounts of a time when those strategies had been implemented. Thus, mirroring Section II, we divided this section into four subsections to display the strategies and stories of FNB Clarksdale with respect to training and technology. We interviewed bank executives, asking about managerial strategies for training and developing current employees, especially with regard to the implementation of new technologies. Additionally, we discussed the current and expected challenges faced by the bank with respect to rapid changes in technology in the industry. Finally, we illustrated the implementation of the strategies by telling stories of bank successes and failures in these realms. Ultimately, in conducting this examination, we aimed to assess the effectiveness of FNB Clarksdale in closing the technological gap between community and regional-to-national-sized banks and warding off the threat of being acquired by a larger, more technologically sophisticated bank.

Section III.2: Training Strategy

The training strategy of FNB Clarksdale has included the cross-training of employees in the understanding of multiple roles as mentioned in Section II.2 and the further development of senior-level officers with additional education. FNB Clarksdale employees typically have received on-the-job cross training but may have received additional virtual compliance training. This training strategy has served the bank well in allowing for the reduction of unnecessary or inefficient hires to reduce overhead costs and has prepared employees to perform more effectively. Bank management has preferred that an employee learn multiple job functions before assuming a new role; this training has been preferred because the understanding of operations, compliance, and needs of various departments has allowed an employee to serve his or her coworkers, and inevitably the customers, more effectively. Further, FNB Clarksdale management has believed that career development is a continual process. Thus, if an employee has stood out among peers to bank management, he or she would be given the opportunity to attend banking school. Most senior officers had completed further training from the Graduate School of Banking at either Louisiana State University or the University of Wisconsin at Madison, which have provided excellent career development skills for bank management.

Section III.3: Training Storytelling

The training needed for the implementation of the Paycheck Protection Program (PPP) required flexibility and teamwork on behalf of FNB Clarksdale management, employees, and other community bankers. Much of the training was done real-time, meaning that FNB Clarksdale management had to read regulations and guidance as it was released by the federal government. Management defined and gave roles to specific departments to ensure effectiveness. However, because the implementation of PPP was unprecedented, the bank saw a high level of camaraderie and assistance from other community bankers; when management had questions, it relied on other bankers and returned the favor to any who needed further assistance.

Section III.4: Technology Strategy

The technology strategy of FNB Clarksdale is to implement new technologies in response to customer demand rather than offer new features before customers ask. This reactive strategy is available to FNB Clarksdale because of the loyalty of the customer base and the strong relationships between bankers and the community. Management does not have to assume whether or not a certain technology is desired; it knows demands of its customers and responds to those demands. Costs of technological implementation can accumulate quickly for community banks, the weight of which is felt intensely, but this strategy allows FNB Clarksdale to avoid incurring unnecessary costs in offering technologies that are not in demand.

One of the greatest challenges with implementing new technology among community banks, and especially for FNB Clarksdale with its relatively small asset size, is determining if the demand for the technology is sufficient to justify the cost of implementation. The customer base in Clarksdale is much less sophisticated than that of Oxford, meaning they have a lower level of technological expertise, and thus the customers do not require a high level of technological implementation to be satisfied with the financial services provided by the bank. For this institution, demand for a certain technology may be more prominent for Bank of Oxford customers than for those of FNB Clarksdale.

Another challenge faced by FNB Clarksdale is the consideration of increased exposure to fraud risk. Community banks typically do not face much fraud risk as a positive result of the strong relationships built with customers over the years. However, as technological advancements offer customers the leisure of remote financial services, FNB Clarksdale is aware of the increase of the risk of fraud that may arise as customers use in-person services less often.

In order to respond to varying levels of customer expertise, minimize costs, and mitigate fraud risk, FNB Clarksdale management collectively develops a full understanding of total demand, upfront and accrued costs, and total risk before implementing a new technology. In addition, in order to keep operations cost-effective and low-risk, the bank keeps one employee in a technological services role but outsources other needed services from vendors.

Section III.5: Technology Storytelling

FNB Clarksdale implemented Apple Pay in 2016, making the bank one of the first in its market to do so. The management decision to implement Apple Pay came with the cost-effectiveness and payment processing security that Apple Pay provided over other yet-to-be-implemented technologies, like mobile deposit, which have required a more stringent weighing of fraud risks and costs for the bank. Rather, Apple Pay, like the recently-implemented EMV chip technology, serves to reduce debit card fraud risk for FNB Clarksdale. One of the few challenges with the implementation of Apple Pay was the authentication of cards, in which customers would need to contact the bank to verify the card; however, the number of calls subsided over time with the saturation of the customer base with the technology. Another challenge was the training of less sophisticated customers to be able to use the technology effectively. However, this challenge was also a great opportunity for the bank to strengthen its relationships and establish trust with those customers; upon training, they received the technology with fascination at the ability to make a payment without reaching for a physical wallet. Looking forward, the bank is looking to continue implementing mobile deposit financial technology and making innovative banking possible for its customers.

Apart from implementing financial technology to serve its customers, the bank has also seen increased flexibility in remote work possibilities with operational technologies implemented following the pandemic. Recently, these technologies made possible the move of the head of Human Resources for the bank from its FNB Clarksdale branch to the Bank of Oxford branch. She is able to remain connected to executive management in Clarksdale in ways she would not have been before the pandemic, making the transition between bank branches seamless.

Section III.6: Training and Technology Summary

In this section, we find that FNB Clarksdale deliberately cross-trains employees in order to cut costs and improve bank efficiency. We also find that the bank has a reactive strategy with respect to technological implementations, which augments the priority of customer relationships at FNB Clarksdale. We find that customer demand for financial technologies varies between bank branches and that operational technologies have improved flexibility for employees who need or desire to work at the other branch.

We discuss the stories of the immediate PPP training given during the COVID-19 pandemic and the rollout of Apple Pay, the most recent financial technology implementation of the bank. We find that the bank faces challenges in quantifying demand, determining costs, and exacting fraud risks of new technologies. We find that the bank faces an additional challenge in training less sophisticated customers once new technologies are implemented. Conclusively, we decide that because the bank does not desire to grow, the need to outpace regional or national banks with technological implementations does not appear to be cost-effective given the sophistication level of the customer base perceived by management.

CONCLUSION

In an industry marked by frequent consolidations and constant technological transformation, community banks must strategically manage profitability, risk management, and the threat of acquisition. In *Section I: Financial Analysis*, we found that the bank should continue to improve earnings performance in its strategic conversion of core deposits to loans. In *Section II: Staffing and Succession*, we depicted the strategies and stories of FNB Clarksdale with respect to recruiting competent and fresh talent and planning for the loss of any key executives. In *Section III: Training and Technology*, we discussed the strategies and stories of FNB Clarksdale with respect to the development of current employees and the decisions to implement new technologies.

We conclude that while many community banks like FNB Clarksdale have experienced an opportunity to drive profitability from a surge in core deposits and a rising rate environment following the COVID-19 pandemic, many risk management factors coming from scale disadvantages, like the high capital levels and low LDR, make it difficult for community banks to compete with regional or national banks and ultimately leave them at risk of takeover. Lacking the ability to compete well puts many community banks in a tough spot for profitability, and if profit margins are small, growth can seem risky. In a consolidating industry, community banks should be looking for strategic ways to grow, avoiding concentration on one geographic area or loan type in order to combat consolidation; if a bank fails to do so, it risks becoming another bank's acquisition target in an effort to diversify.

This case study raises further potential topics of interest for banking stakeholders. With respect to management of financial institutions, further research can be done investigating the effects of the rising rate environment on various loan portfolios, considering the strategic advantages of having a number of agricultural loans during such a time. With respect to investors, further investigation of the effects of cross-training and financially incentivising employees on the returns of the firm is an interesting question raised by FNB Clarksdale's operations. Lastly, with respect to bank regulators, further research can be done with respect to finding additional reporting means, like that of the alternative capital levels reporting measure, that may help community banks reduce costs and give more of their attention to what they prize most: building relationships in the communities they serve.

APPENDIX A

Figure A1: Comparative Earnings Performance of FNB Clarksdale from 2018 to 2022

This figure depicts profitability measures of FNB Clarksdale compared to those of other community banks in Mississippi. Source: FDIC 10-K report as well as UBPR.

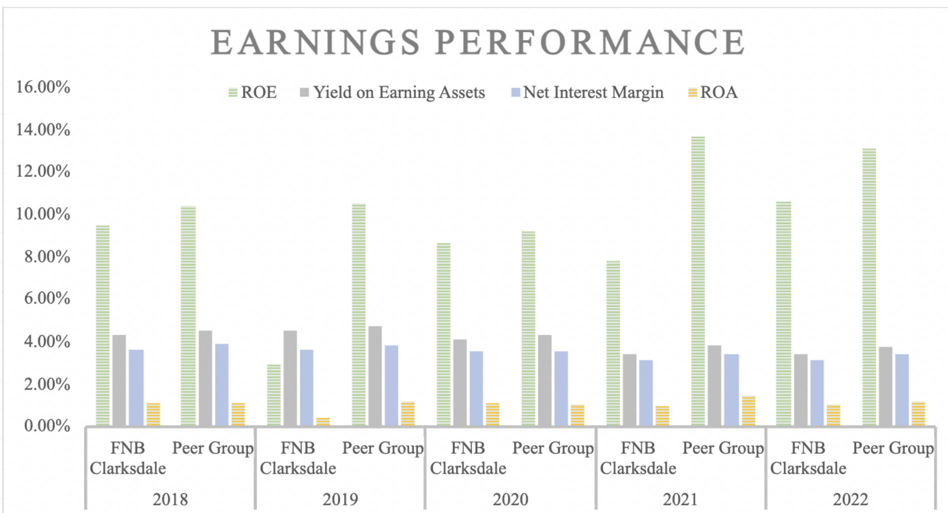

Figure A2: Loan Portfolio Composition of FNB Clarksdale from 2018 to 2022

This figure depicts the loan portfolio composition of FNB Clarksdale as a percentage of total portfolio value. Source: UBPR.

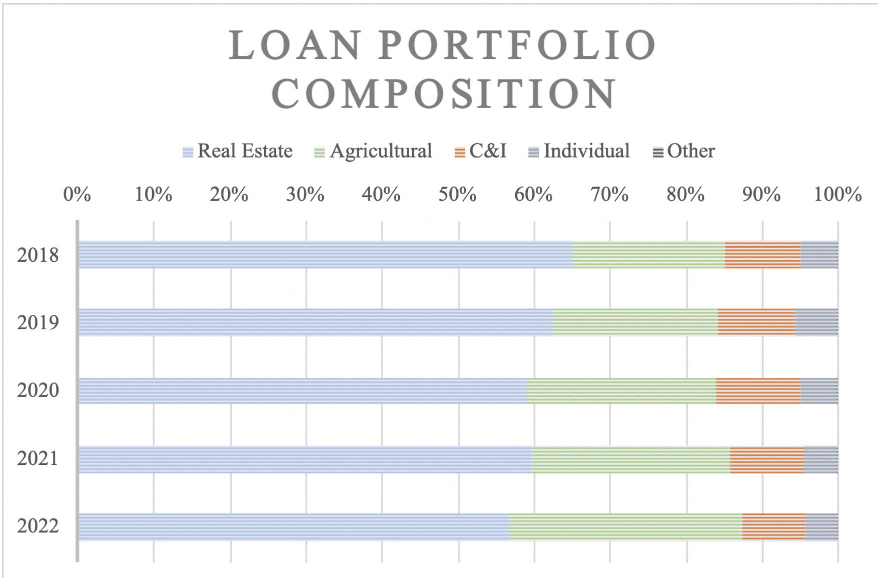

Figure A3: Total Asset Composition and Growth of FNB Clarksdale from 2018 to 2022

This figure depicts changes of total asset composition of FNB Clarksdale. Source: FNB Clarksdale FDIC Form 10-K filing.

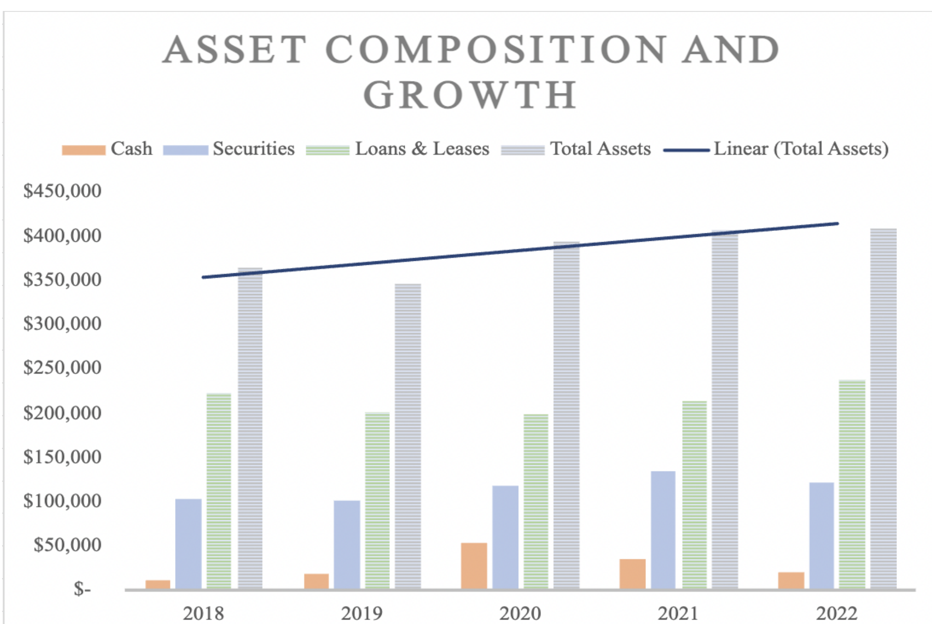

Figure A4: Capital Levels of FNB Clarksdale in 2022

This figure depicts Tier 1 Leverage Ratio and Tier 1 Capital Ratio for FNB Clarksdale in percentage terms, which are benchmarked with CBLR minimum percentages. Source: FDIC, UBPR

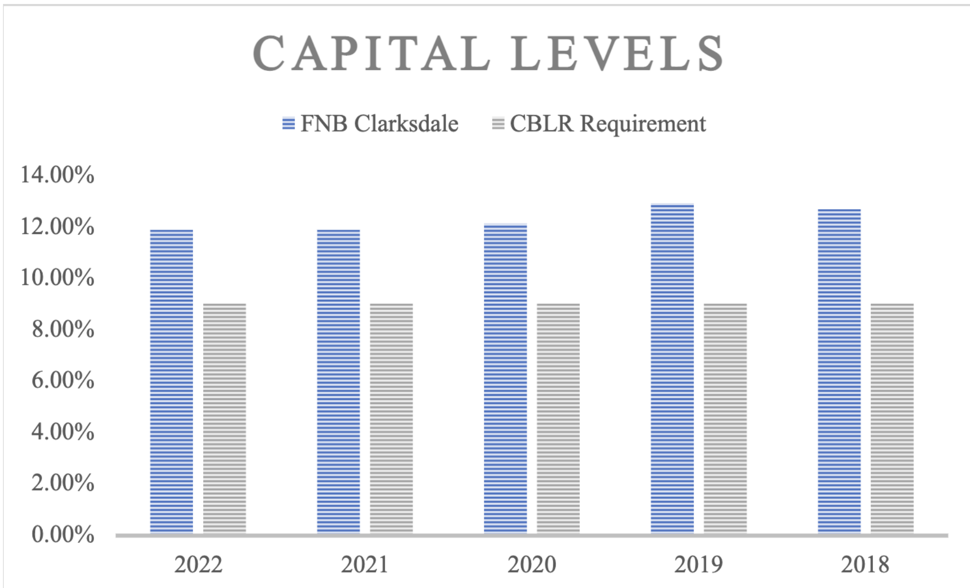

Table A1: Key Financial Ratios of FNB Clarksdale from 2018 to 2022

This table depicts the Key Financial Ratios of FNB Clarksdale in percentage terms. Source: FDIC 10-K and UBPR.

Key Financial Ratios										
	2022		2021		2020		2019		2018	
	FNB Clarksdale	Peer Group	FNB Clarksdale	Peer Group	FNB Clarksdale	Peer Group	FNB Clarksdale	Peer Group	FNB Clarksdale	Peer Group
ROE	10.56 %	13.08 %	7.76 %	13.68 %	8.65 %	9.15 %	2.90 %	10.50 %	9.46 %	10.34 %
ROA	1.01 %	1.19 %	0.93 %	1.43 %	1.13 %	1.02 %	0.38 %	1.16 %	1.12 %	1.10 %
Net Interest Margin	3.15 %	3.43 %	3.14 %	3.42 %	3.54 %	3.53 %	3.59 %	3.81 %	3.60 %	3.90 %
Yield on Earning Assets	3.43 %	3.74 %	3.39 %	3.83 %	4.07 %	4.28 %	4.48 %	4.73 %	4.31 %	4.54 %
Loan-to-Deposits	65.70 %	63.66 %	59.82 %	61.80 %	57.82 %	67.44 %	67.04 %	75.37 %	70.48 %	77.89 %
Loan-to-Assets	58.10 %	55.81 %	52.64 %	53.98 %	50.47 %	57.74 %	57.74 %	64.27 %	61.39 %	65.95 %
Leverage Ratio	12.36 %	10.86 %	11.90 %	10.14 %	12.09 %	10.18 %	12.89 %	10.85 %	12.69 %	10.84 %
Equity Capital-to-Assets	8.27 %	8.51 %	11.48 %	10.25 %	12.17 %	10.77 %	13.23 %	11.32 %	12.37 %	10.78 %
Asset Growth	0.40 %	5.10 %	3.29 %	10.35 %	13.74 %	-2.33 %	-4.81 %	5.29 %	0.00 %	0.00 %
Loan Growth	10.81 %	8.65 %	7.73 %	3.17 %	-0.59 %	-12.26 %	-10.47 %	2.61 %	0.00 %	0.00 %

APPENDIX B

This Appendix Contains the 2023 Community Bank Case Study Competition as Given by the Conference of State Bank Supervisors

CSBS

2023 Community Bank Case Study Competition

Background

Banks provide credit and financial services in the United States. Community banks play a vital role in sustaining their local economies and are key providers of banking services, particularly in rural communities across the country.

Today's community banks face a multitude of challenges, including a competitive jobs market, succession issues, and meeting changing consumer needs. Consolidation in the community bank industry is an ongoing concern. During the past decade, the number of community banks has declined by roughly one third. The steady decline in the number of community banks and their share of U.S. banking assets have raised questions about the future of community banking.

For the 2023 CSBS Community Bank Case Study Competition, teams will be asked to learn about how management and the board of directors of their chosen institution are (1) recruiting, training and retaining talent, (2) approaching succession planning and demographic changes in their area, and (3) using technology to advance their operations.

Through this study, we hope to get a better understanding of how community banks are positioning themselves for success and sustainability in a fast-changing banking environment.

Questions – 2023 Community Bank Case Study Competition

Part I: Financial Analysis

Using the FFIEC 041/051 Call Report, Uniform Bank Performance Report (UBPR), and other publicly available data sources, students should analyze and provide an analysis of the following:

- Earnings Performance
- Loan Portfolio Composition
- Asset Growth
- Capital Levels
- Liquidity

To facilitate uniform analyses amongst teams, this financial analysis should be completed on a year-over-year basis covering five years.

Part II: Staffing (address the questions most pertinent to the institution)

1. How has the bank recruited and retained talent through the years? Were new benefits added at some point to stay competitive? What does bank management say makes them stand out as a great place to work? What do you, as an outsider observer, think makes the bank unique?

2. The pandemic brought with it a historically strong and competitive labor market, how does the bank plan to differentiate itself from competitors on staffing in this unusual environment? For example, does the bank taps into a local university for recruitment efforts or has unique benefits it offers staff?

3. Describe the community bank's staff generational makeup (Gen Z, Millennials, Gen X, Boomers, etc.). Was there significant turnover during the pandemic? If yes, what did bank management glean from exit interviews?
4. In the past decade, has the bank made any notable hires that provided new expertise (such as IT) or new perspective that management would like to highlight? How did the institution manage to recruit that/those individual(s)?
5. Has the bank dealt with the exit of any senior executive officer(s) in the past decade? How did the bank's succession plan help it respond to that exit?
6. How does the bank approach succession planning? (Is it a family-owned institution, shareholder driven. etc.?) What techniques does management use to identify new leaders and successfully manage critical staffing transitions? What challenges do they expect for succession planning? For example, are multiple senior executive officers expected to leave simultaneously for retirement or is it a family-owned and operated bank where the next generation have no interest in banking?

Part III: Training and Technology (address the questions most pertinent to the institution)

1. What training (leadership, or job functional certifications) does the bank provide staff or senior leaders? How does the bank provide career development for younger staff?
2. The pandemic made hybrid work a mainstay for many employees. Has the bank provided post-pandemic flexibility in work location for any portion of its workforce?
3. What new technologies has the bank adopted in the past five years? What were some of the key challenges with implementation? How are staff trained to handle new technology and questions from customers?
4. What one great story does the bank have that exemplifies a community bank having a technological success in the past five years?
5. Has the bank been examined since the pandemic began? Does management prefer having examiners onsite or remote?

   For example, is the bank considering partnering with fintech companies to provide services that they cannot produce in-house?
6. How is the institution using technology to drive profitability? For example, a technology that opens a new revenue stream, or a chat bot on its website.

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