

## Central Pennsylvania's new banks prosper in downturn

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By Tim Stuhldreher

You might think the worst financial crisis since the Great Depression would be a bad time to be running a startup bank.

But leaders of the midstate's de novo institutions say their newness and community focus give them a competitive advantage.

"We've come through difficult economic times. ... In some ways, that has created some benefits," said Mike Kochenour, president and CEO of [York Traditions Bank](#), founded in 2002.

"De novo" is Latin for "from the beginning." Strictly speaking, it refers to banks five years old or less. But banks continue to make key decisions through their first decade on growth strategies and market penetration, decisions that shape the kind of institution they end up becoming.

Bank	Founded	Branches	Assets (millions \$)
Centric	2007	2	\$182.1
Graystone Tower	2005	27	\$1,585.4
Integrity	2003	7	\$534.1
Province	2000	1	\$103.6
York Traditions	2002	4	\$228.6

SOURCE: FEDERAL DEPOSIT INSURANCE CORP.

De novo banks are capturing customers given short shrift when large banks absorbed many of the region's community banks about a decade ago, said Jim Gibson, president and CEO of [Integrity Bank](#), founded in 2003.

The near-collapse and bailout of the nation's largest banks over the past few years renewed customers' appreciation of the benefits of banking locally, Gibson, Kochenour and others said.

"As a result of the tough climate, people have tended to want to leave larger institutions," said Andrew Samuel, president and CEO of [Tower Bancorp Inc.](#), the holding company of [Graystone Tower Bank](#), founded in 2005. "It has actually spurred our growth."

There will always be certain deals that, due to their scope or complexity, require the financial might and expertise of large banks. But for people "who want to do business

with people they know,” who value those relationships, community banks are vital, Kochenour said.

York Traditions, Graystone Tower and Integrity Bank all were formed in 2002 or later. Province Bank was formed in 2000 and a fourth midstate bank, [Centric](#), was reorganized and renamed in 2007 — making it a “quasi de novo,” as Centric President and CEO Patricia Husic put it.

In the late 1990s and early 2000s, banks such as Wachovia, [Sovereign](#) and [PNC](#) snapped up midstate banks, including Hamilton, Waypoint and Bank of Lancaster County. [Wells Fargo](#) subsequently bought [Wachovia](#) and Spain’s [Banco Santander](#) bought Sovereign.

As a result of those and other deals, “many folks are now with a bank they didn’t choose,” Gibson said. Staff reassignments or branch closures may have fed their discontent, he said.

Those dissatisfied customers, which included many commercial clients, represented a rich business opportunity. Nevertheless, launching a bank is a daunting task.

A de novo bank requires millions of dollars in capital, an expert and committed management team, and a detailed, feasible business plan. Gaining regulatory approval can take up to a year.

“When I started, I wanted to get the smartest people I knew,” said Gibson. That is a sentiment others echoed.

Finding good talent became harder once banks began scaling back their training programs in the 1990s, said [George Millward](#), a banking consultant who was on the executive team that founded Millennium Bank, a de novo bank that opened in Malvern, Chester County, in 1998.

The last generation to go through those programs are in their 40s now, said Millward, who heads Millward Consulting in Berks County.

De novo openings normally take about 18 months, Samuel said. Graystone Tower’s took less than six months, a speed he attributed to the firm’s sense of mission.

Unlike a true de novo, Centric had legacy issues to resolve, Husic said. When she and a team of local investors bought and rebranded Vartan National Bank as Centric, they had to go through Vartan’s lending portfolio loan by loan and negotiate numerous modifications, she said.

“It’s a lot easier starting with a clean base,” she said.

## **Different strategies**

The midstate's de novos all build their business around community banking and relationship banking, their leaders said — in other words, forging close ties with customers and trying to meet as many of their banking needs as possible.

That's the right strategy, said banking consultant Jay Brew, CEO of BNK Advisory Group, based in Bethlehem.

De novo banks in states such as Georgia and Illinois got caught up in the real estate bubble, he said. Lenient regulators let them pour funds into high-risk land development and commercial real estate projects, he said. Those banks "have been at the top of the failure list," he said.

Many community banks, not just de novo banks, went that route, Millward said.

In Pennsylvania, effective bank regulation and a more diversified economy kept de novo banks much healthier, Brew said.

The first priority of any de novo bank is growing its loan portfolio, and the expertise of its management team will determine how it does that, Millward said.

The greater challenge, and the key to long-term success, is moving past the focus on loans in the medium term and growing a customer deposit base, he said.

Branch openings are one sign that banks are connecting with retail customers. Integrity Bank opened two branches in Lancaster County this month, its sixth and seventh. York Traditions Bank opened its fourth branch in September. Centric began building its third branch this month.

Graystone Tower has grown rapidly thanks to two acquisitions. It added 16 branches when Graystone Bank bought Tower Bancorp last year, and will acquire 23 more when it completes its acquisition of [First National Bank of Chester County](#), expected by the end of this year.

Apart from acquisitions, Graystone Tower will open four branches and a loan production office by the end of 2010, though it is closing three branches, too.

Graystone Tower's first priority is organic growth, but it complements that with "strategic deals," Samuel said. The goal is a franchise extending about two hours' driving distance from Harrisburg in all directions, he said.

Graystone Tower has been "thoughtful" about its acquisitions strategy and has had the resources to execute it, Millward said.

Province is the oldest but smallest of the group, with three branches and \$103.6 million in assets.

The bank's philosophy is conservative, and it likes lending in markets with "staying power, such as multi-family residential properties, President and CEO Greg Diehl said.

"We're happy with the way we grew the bank, (though) we wish we could've grown a little faster," he said.

Province may get renewed momentum when it absorbs troubled Union National Community Bank, which has 10 branches, all in Lancaster County, and \$500 million in assets. The two banks announced the move in April and are awaiting regulatory approval.

If the economy cooperates, Province could be a billion-dollar bank in five years or so, Diehl said.

## Variations on a theme

There are different ways of pursuing a "relationship banking" model. Integrity Bank's Gibson has adapted and refined the strategy of Commerce Bank/Harrisburg, now [Metro Bank](#), where he was president for 14 years. Metro is well-known for its retail banking model, high-impact branch design and focus on customer amenities such as evening and weekend hours and free coin counting.

Gibson has added further innovations, such as a three-step drive-through system that significantly reduces customer wait times.

"Sixty-one percent of transactions are drive-through," he said, yet most banks have more in-bank teller positions.

Often they put an ATM in the first drive-through position, dramatically reducing the value of a key point of customer contact. Integrity's ATM is at a separate, unstaffed drive-up spot on the other side of the bank.

Integrity achieves efficiency by maximizing volume at each branch — up to six times the industry average — rather than branching prolifically, Gibson said.

Branch design, customer service, and rates all work together to give the bank a strategic advantage, he said.

York Traditions began with "a keen focus on family business and small business," expecting that business owners would turn to the bank in time for personal banking for themselves and their families as well, Kochenour said.

"That was part of our strategic plan," he said.

Centric Bank is building both its business and retail customer bases, expanding online services as part of its strategy to attract the latter, Husic said. Adding branches will help build the retail side, she added.

Besides relationship-based retail and small business clients, Graystone Tower has products and services tailored specifically to nonprofits, Samuel said.

The bank has reached out to all three markets “from day one,” he said.

Province is owned by Donegal Insurance Group, and part of its strategy was to “take advantage of any synergy in the insurance market,” Diehl said.

“That was slow to start, but we finally got some traction,” he said.

In many cases, de novo banks can offer customers newer technology than their older competitors. Lacking outdated systems and their sunk costs, they can hit the ground running with the most up-to-date equipment.

However, technology is getting cheaper, and it no longer offers a decisive competitive advantage, because it’s comparatively easy for other banks to acquire equivalent systems, Millward said.

In Centric’s case, Vartan had done a system conversion shortly before the acquisition, so “we did have state-of-the-art technology,” Husic said.

## **The future**

The midstate likely won’t see any de novo banks forming for awhile.

The [Federal Deposit Insurance Corp.](#) issued three to six bank charters in Pennsylvania every year from 2003 to 2008, but has issued none since.

“The regulators have made it known there’s no way they are going to approve a bank charter” until conditions improve, and future de novos will face higher capital requirements, Brew said.

Husic said more quasi de novos like hers — buying and turning around a troubled institution — may become more common as a result.

“We were ahead of the curve and didn’t know it,” she said.

All four bankers said their institutions are well positioned for growth as the economy recovers. They know they will face additional compliance burdens as the federal financial reform bill is implemented, but said they’re confident they can manage.

Having started their banks as alternatives to larger ones, they all stressed the importance of staying true to their community roots.

“I wake up every morning seeing this as a tremendous privilege,” Kochenour said.