CSBS 2022 National Survey of Community Banks

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Findings from the 2022 CSBS National Survey of Community Banks Presented at the 10th Annual Community Banking Research Conference

Sept. 28-29, 2022

Foreword from Tom Fite

Inflation rates are at their highest level in more than 40 years. Economic growth is stagnant. The pandemic continues to linger and geopolitical tensions have intensified.

These economic uncertainties are playing out across the nation. Net interest margins—followed closely by economic conditions—ranked as the top external concern in our ninth annual Conference of State Bank Supervisors National Survey of Community Banks.

Cybersecurity remains the top internal challenge, although it dropped by 16% from last year as a very important risk, perhaps indicating banks are more prepared.

Staffing concerns continue to rise. This year, nearly 85% of respondents said retention was an extremely or very important issue, a 10% increase from last year.

Meanwhile, we see a continued interest by community banks to add more technology to the relationship-lending model. The percentage of community bankers who said adoption of new technology is very important doubled in the last three years. However, high costs related to technology remain a concern.

Regardless of challenges, both new and old, community bankers expect the strength of relationship-based lending to expand more than transactional lending. To me, that shows the value of community banks and the important role they play in serving their customers and communities.

I invite you to read the full report and learn more about what community bankers say are their most important issues.

Tom Fite

Chair, Conference of State Bank Supervisors
Director, Indiana Department of Financial Institutions

2022 CSBS National Survey

Introduction

This year's National Survey of Community Banks, conducted by the Conference of State Bank Supervisors (CSBS) and state regulatory authorities, was distributed during a period of economic upheaval. Consumer prices and interest rates were rising. Asset prices and economic output were dropping.

In previous years, challenges faced by bankers tended to be episodic, such as implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) or providing lending lifelines for businesses during the COVID-19 crisis. This time around, on the 10th year of the conference, the challenges are macroeconomic. They appear to be more pervasive and more traditionally cyclical in nature. They underscore what the late John Ryan, then president and CEO of the CSBS, referred to 10 years ago as the "push and pull of local, national and global forces."

Other issues extend beyond the economy. Two of them, particularly, were previously identified by Jerome Powell, now chair of the Board of Governors of the Federal Reserve but then a Fed governor, in his remarks at the first conference: (1) technology, which "changes the way consumers interact with their banks"; and (2) competition from nonbank providers of financial services, which "moves customer interaction outside of the traditional banking system." Both are as topical now as they were then.

This survey was launched the second year of the conference. Each year, some questions are added to the survey, reflecting emerging, and perhaps temporary, issues, while others fall off, as interest in them wanes. But many questions have been asked nearly every year.

Our report also incorporates extensive comments based on interviews that were conducted with five community bankers from across the United States. Transcripts of the complete interviews can be found in the last section of this report.

Background

To develop the 2022 national survey, CSBS staff met with key academic, industry and regulatory stakeholders to identify current issues of relevance to community banks. The survey was distributed by the state banking regulatory authorities from April to July 2022. The number of respondents was 498.

All the participating institutions had less than $10 billion in assets, a benchmark for community banks established under Dodd-Frank. The vast majority were state-chartered banks. For ease of exposition, all surveyed entities in the analysis that follows will be referred to as "community banks."

We acknowledge certain limitations of the survey:

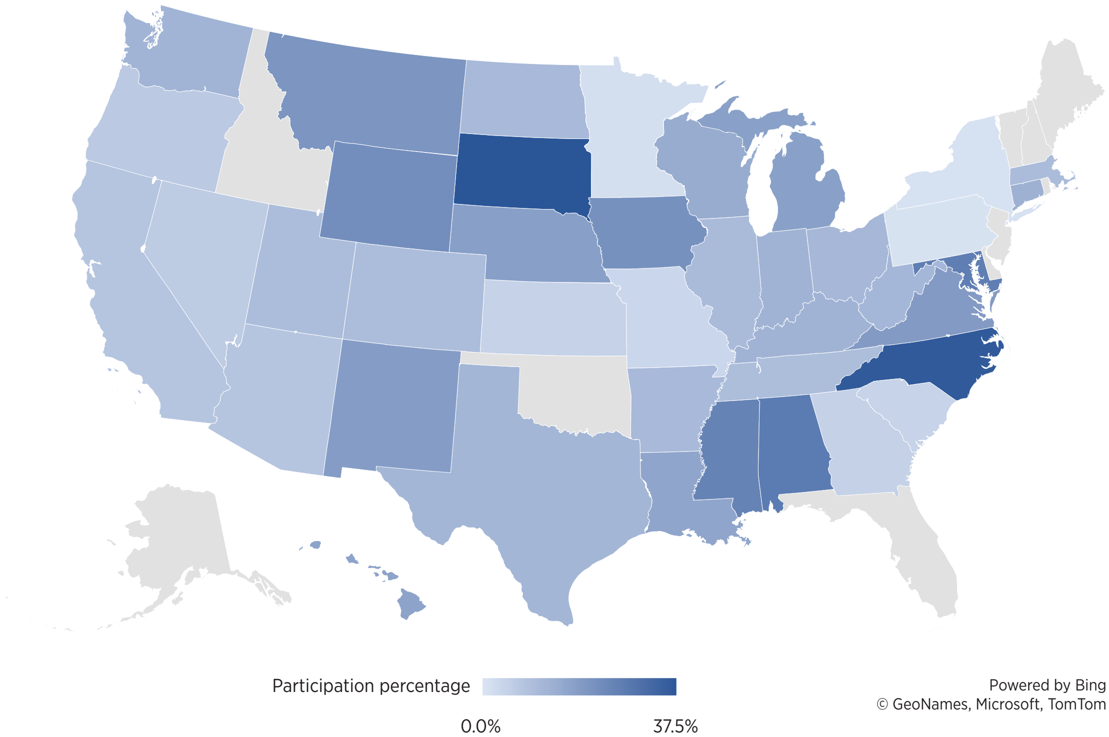
- It was not completed in every state.
- Respondents participated on a self-selected basis.
- Banks did not necessarily respond to every question.
- Detailed statistical testing, which would be required to definitively quantify the extent to which surveyed banks were representative of the overall industry, was not conducted.

Conclusions must be qualified accordingly. Because each respondent did not answer every question, responses are expressed as percentages of respondents to specific questions. Due to rounding, not all percentages will add up to exactly 100.

Key Findings

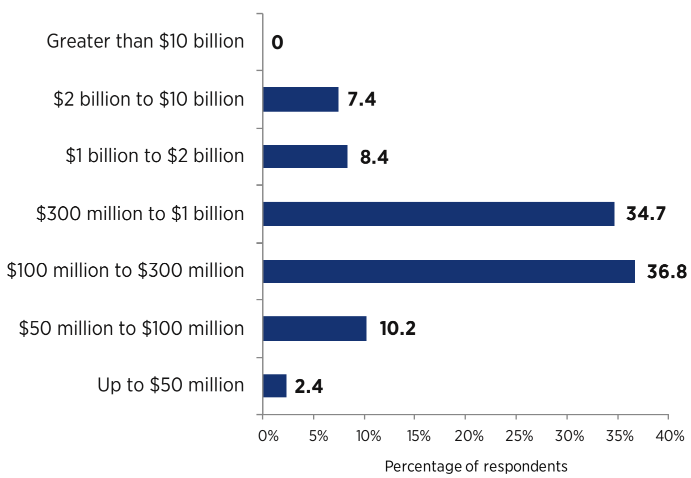
- Economic conditions and net interest margins were ranked by community bankers as their top external risks. While net interest margins ranked first in importance among external risks, they were not considered more worrisome than a year ago.
- Cybersecurity ranked first in importance among internal risks, as well as in current and future technological challenges.
- Inflation was described as a persistent, but manageable, challenge.
- Community bankers expect relationship-based lending to expand more than transactional lending.
- The percentage of bankers who said adoption of new technology is extremely important doubled in the last three years.
- Although cryptocurrency services are offered by only 1% of surveyed banks, bankers are equally divided on whether such services are important or unimportant.
- Community bankers are worrying less about competitive risks than they did a year ago.
- Compliance costs at community banks continued at levels that have persisted for several years.
- In-house provision of core processing services, compared with services provided externally, was viewed by bankers as cheaper but less secure.

FIGURE 1
Survey participation rate by state



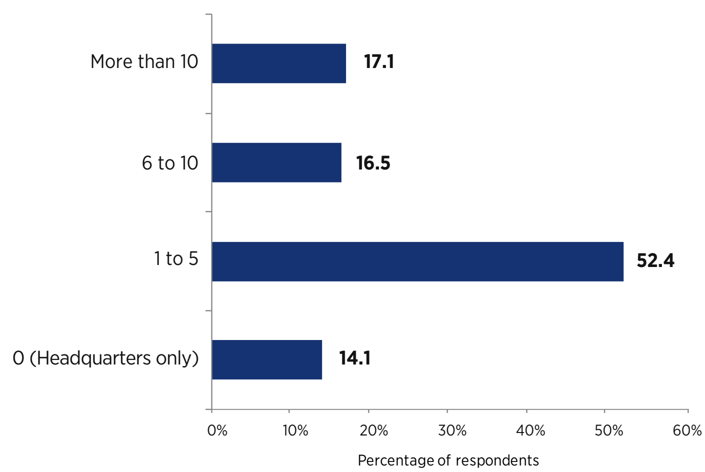
Participants came from 40 states. This year was the first year that California participated. The participation rate was highest in South Dakota. Iowa had the largest number of respondents with 55 banks responding.

FIGURE 2
Asset size of surveyed banks



Of the banks surveyed, 13% had assets less than $100 million. Most banks fell in the category of $100 million to $300 million.

FIGURE 3
Number of branches of surveyed banks



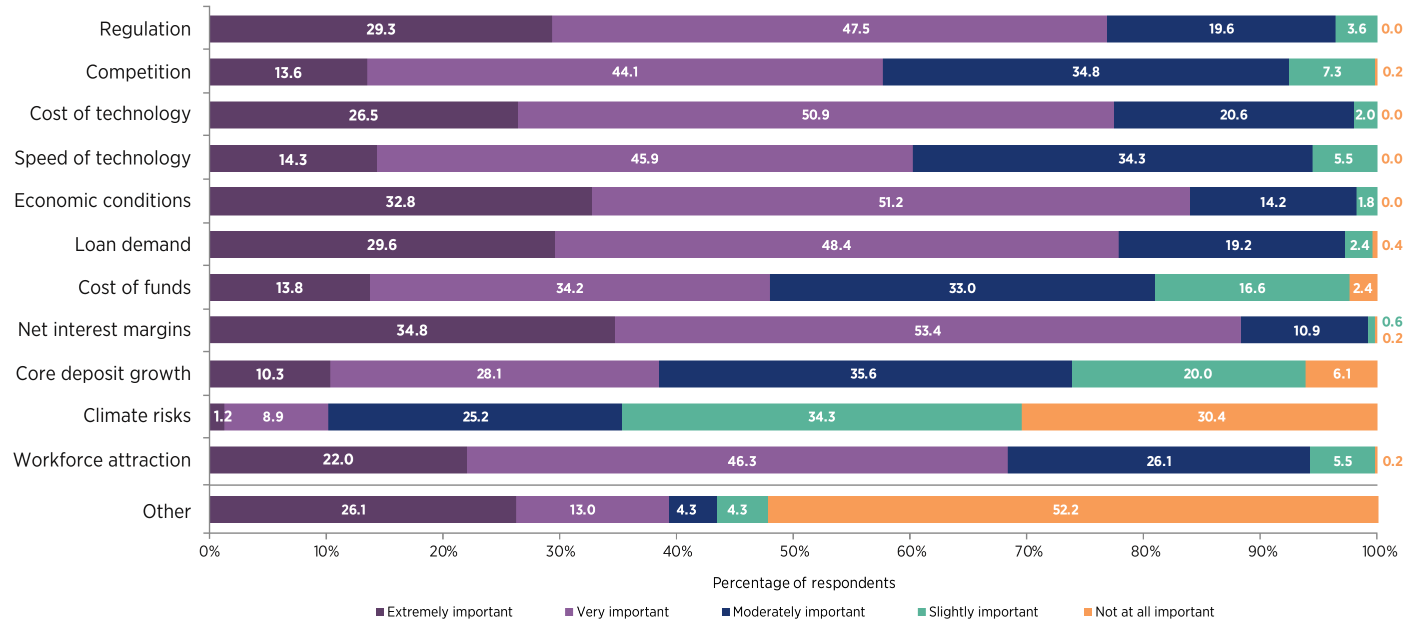
Although more than half of all banks had between one and five branches, significant dispersion is evident by the 14% of banks with no branches and the 17% with more than 10 branches.

At the time the survey was distributed, the U.S. economy was on a precarious footing, following a first-quarter decline in gross domestic product of 1.6%, which was in sharp contrast with the increase of 6.4% recorded in the same quarter last year. Community bankers who took this year's survey noted that in addition to economic conditions, they face a range of many other external risks that includes net interest margins, loan demand, technology costs and regulation.

Upon answering "extremely important" to a particular category, bankers were then asked to rank the importance of these external risks. A given category was ranked first if it was named most often as the first or second overall risk.

FIGURE 4

How important are the following external risks to your bank today?



Net interest margins were named by 35% of bankers as "extremely important" and by 53% as "very important." They ranked first in importance among external risks. Nevertheless, this relatively high level of assessed risk was lower than last year's despite increasing interest rates—the 10-year Treasury yield was above 3% at the time of the survey, about twice as high as it was a year earlier.

Economic conditions were named by 33% of bankers as an "extremely important" external risk and 51% as "very important." However, economic conditions were ranked second in importance among all external risks behind net interest margins.

Loan demand was identified as the third-ranked external risk. Although 30% of bankers described it as "extremely important," it was lower than what was reported last year. Loan demand was selected as a "very important" risk by 48% of respondents. Concerns with external conditions in lending markets were not necessarily increasing despite ongoing economic turmoil.

Bankers' Perspectives: Interest Margins Become Interesting Again

Our asset liability committee meetings are fun again. We are having significant conversations about our position relative to increasing costs of funds, what we need to do to maintain competitiveness, what our loan yield is and where our targets are. Volatility provides opportunity for us to increase our net interest margin, but it also is an opportunity where we may be on the wrong side.

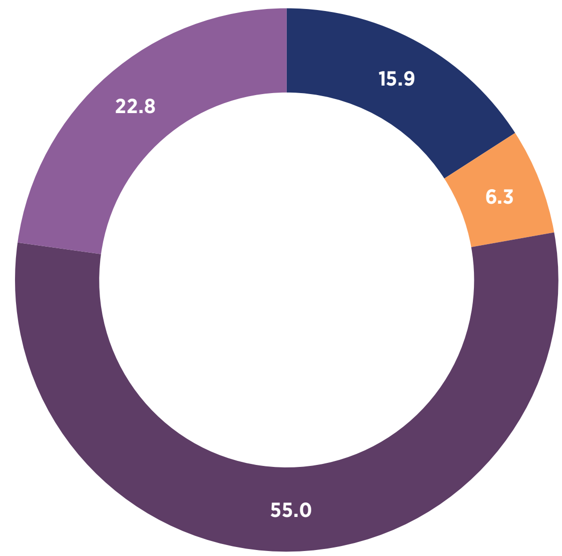
–Joseph W. Conover, Northwest Bank, Spencer, Iowa

The Risk of Inflation

Bankers were asked how inflation creates challenges for their banks; 55% of respondents thought that inflation was likely to persist, but they indicated that they were able to manage inflation challenges. If this is the case, this would be consistent with predictions that inflation could have a positive impact on bank profits extending into 2023. Nearly 23% of bankers thought inflation was likely to persist but would be difficult to manage. Overall, nearly 78% of bankers viewed inflation as likely to persist. Inflation has the greatest impact on personnel expenses.

FIGURE 5

How does your bank view inflation challenges?



Additional External Risks

- Technology imposes risks as well as creates opportunities: The cost of technology and implementation of technology were named by more than 26% of bankers as "extremely important." Less concern was expressed for speed of technology.
- Less than 14% of bankers said that risk of competition was "extremely important," down considerably from the 38% reported last year. Competition ranked near the bottom of external risks.
- Two years ago, prior to the pandemic, core deposit growth was named most often by bankers as their greatest challenge, while the cost of funds was identified as the biggest influence on profitability. This year, 10% and 14% of bankers, respectively, described these factors as "extremely important."
- One question was asked this year to address a risk potentially rising in importance, particularly in a year of an increased magnitude of extreme weather events around the world. Although climate risk ranked last in importance among external risks, about 70% of bankers considered it to be important to some degree.

INTERNAL RISKS

Each bank faces risks that are unique to its operation, but some themes carry across all banks. Figure 6 represents the choices of respondent banks that were asked to indicate the internal risks they view as important.

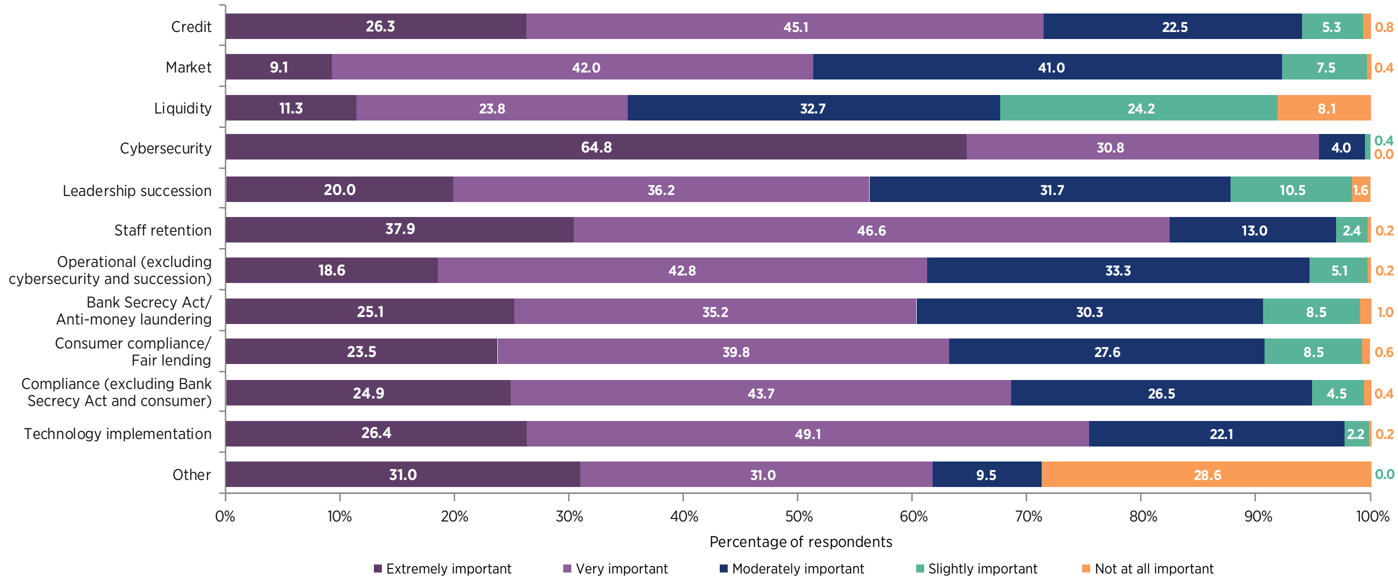
Cybersecurity risk was named by nearly 65% of bankers as an "extremely important" internal risk, which was lower than the 82% reported last year—perhaps reflecting better preparation by the banking industry to combat fraud and corruption—but still ranked first in importance among internal risks. An additional 31% named it as a "very important" risk.

Staffing retention was selected by 38% of bankers as "extremely important," noting it as the second most important internal risk facing their banks. An additional 47% named staffing retention as a "very important" internal risk.

Credit risk ranked fourth among bankers who chose it as an "extremely important" internal risk. About 26% of bankers considered it so, compared to 45% last year. The decline presumably reflects continued reductions in noncurrent loan ratios to near-record lows. Of those, credit was ranked fourth in importance among internal risks. An additional 45% named it as a "very important" internal risk.

FIGURE 6

How important are the following internal risks facing your bank today?



Additional Internal Risks

- Consumer compliance and compliance in general were considered to be less important. For the former, 24% of bankers this year and 28% of bankers last year considered it "extremely important," while for the latter, the same points of comparison were 25% and 24%, respectively.
- The concern about leadership succession was relatively low, with only 20% of bankers considering it to be an "extremely important" risk. This suggests that consequences of poor succession planning may not be as dire as anticipated; seven years ago, for instance, succession issues were forecast to be "the biggest tsunami to hit community banking starting in just a few years," according to one survey respondent.
- About 61% of bankers said operational risk (excluding cybersecurity and succession) was either "extremely important" or "very important," which is slightly lower than what was reported last year. It ranked low among internal risks.
- Compared with last year's survey, banker perceptions of operational risks declined across many categories, including cybersecurity, credit and operations (outside cybersecurity and succession). This presumably reflects, in part, lessening impacts of the pandemic.

Bankers' Perspectives: Good Employees Are Hard to Find

Historically, community banks were successful at recruiting (employees) away from larger banks. But as larger banks have become more "siloed" in their loan processes, it has been increasingly challenging to locate bankers with the well-rounded knowledge of "cradle-to-grave" lending that is vital to relationship banking. We are taking steps to keep the relationship model alive and well using the workforce available to us.

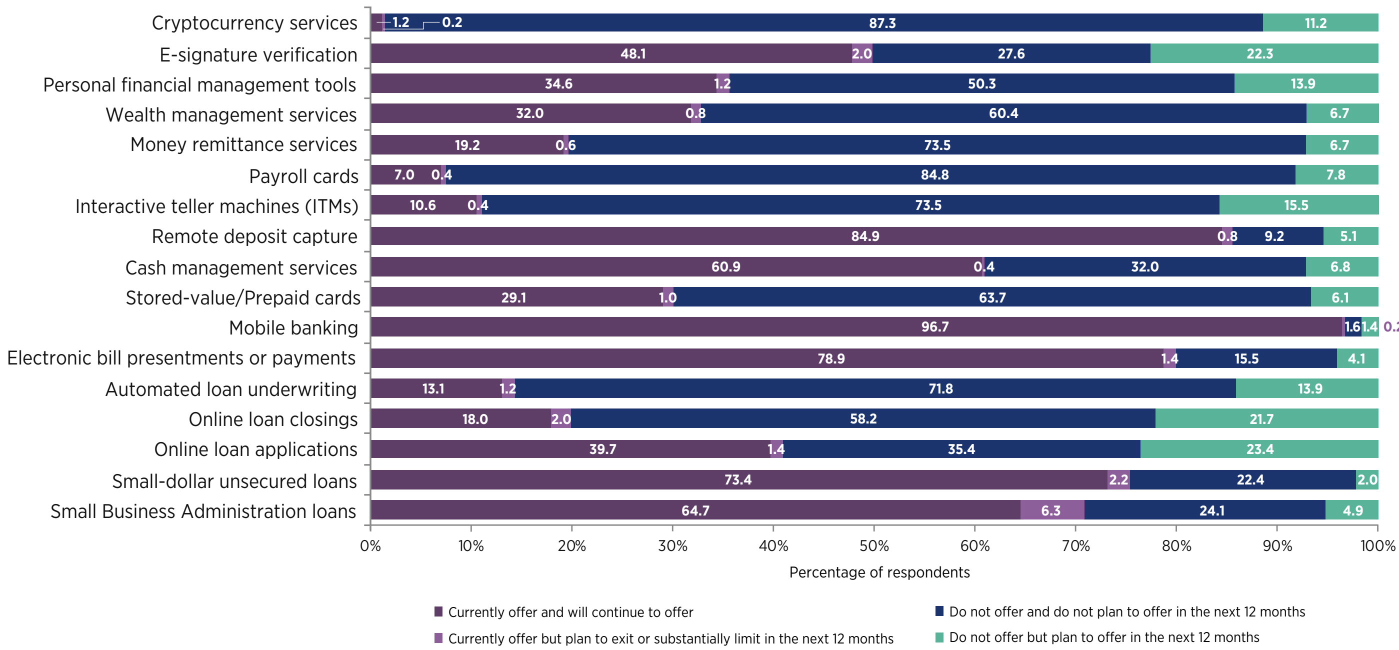
–Janet Silveria, Community Bank of Santa Maria, Santa Maria, California

It is difficult for people to join community banking because it's not considered glamorous. In smaller towns, (with) less opportunities, people may opt for it. In bigger cities, it's more of a problem.

–Saleem Iqbal, HAB Bank, New York

FIGURE 7

What are your bank's intentions regarding the following financial products or services?



Banks are responding to changing business needs by prioritizing flexibility in online loan products and services.

Figure 7 shows that the highest proportions of banks currently do not offer but plan to offer e-signature verification, online loan closings and online loan applications within the next 12 months. Close to 97% of banks now offer mobile banking services, while nearly 85% offer remote deposit capture, with another 5% to offer it soon.

In nontechnical services in 2022, Figure 7 shows:

- About 33% of banks offered wealth management services.
- About 36% of banks offered financial planning services despite ranking very low on importance; 17% of bankers, in fact, said they were unimportant, and less than 2% said they were "extremely important."
- About 20% of banks offered money remittance services. Sources of primary and secondary competition were dispersed across categories.
- Among other services, 30% of banks offered stored-value cards, 7% offered payroll cards, 61% offered cash management services and 76% offered small-dollar unsecured loans.
- The Small Business Administration (SBA) was a popular vehicle for lending in 2020, under the Paycheck Protection Program, when 77% of banks said they offered such loans. This year, only 71% of banks offered SBA loans—and 6% of those planned to get out, perhaps acknowledging implicitly the emergence of fintechs.

Bankers' Perspectives: Product Lines May Narrow at Some Banks

I am concerned with this narrowing of business lines for community banks, whether it be from competitive pressure or, in the case of mortgage lending, the burden of regulation. It makes it prohibitive for smaller institutions to be in some lines of business full time.

–Joseph W. Conover, Northwest Bank, Spencer, Iowa

A typical community bank, as you know, will be in consumer banking products, residential mortgages, auto loans, and debit cards and everything that a consumer needs. So basically be everything for everybody to whatever extent they can.

Now, the future customers of these banks are millennials and Gen Zers. But it is yet to be seen how much value future customers will give to relationships. Or will they rather prefer anything that has better technology, ease, convenience, AI? What if they prefer to get everything done through their phones, will they really care about having relationships with the bank? Or will they just take out a loan from Google or Amazon or whoever? That is the big question, and only time will tell.

–Saleem Iqbal, HAB Bank, New York

The community banking industry has steadily expanded its offerings of technological services. Some changes are dramatic, as in the case of mobile banking, which was offered by 71% of surveyed banks in 2013, but by 97% last year—a transformation to near universality. Lesser increases are evident in older technologies, such as remote deposit capture, which was introduced following changes in check-clearing regulations in 2004. Offerings of this service increased from 77% to 86% over the last seven years.

Close to 40% of bankers considered technology, whether current or future, to be an opportunity rather than a threat. Only 6% believed the converse. Technology's role, moreover, is expanding; 13% of bankers this year said adoption of new technologies was "extremely important," which was higher than the 6% reported three years ago. Community bankers said they believe the greatest technological opportunities existed in mobile banking services, while cloud-based core systems and fully integrated loan processing systems also ranked highly. Cybersecurity was ranked by more than 71% of bankers as the top future technological challenge, as were spend rates and core processor responsiveness.

Meanwhile, few banks expressed interest in acquiring an online bank or creating an online charter.

Bankers' Perspectives: The Pandemic Accelerated Innovation, but at a Cost

The most significant impact of the pandemic on banks is digital transformation. This created daunting challenges for both banks and customers, but also led to rewarding outcomes. We are better bankers as a result.

The pandemic forced us to challenge our old ways of thinking and redirected our attention to our most pressing priorities, while highlighting areas of marginal importance. We now offer more and better digital and remote interactions, we have better utilization of virtual tools, and we have become more flexible in terms of hybrid and/or remote work opportunities.

–Rogers Pope Jr., Texas Bank and Trust Co., Longview, Texas

FIGURE 8

How does your bank view existing banking technology?

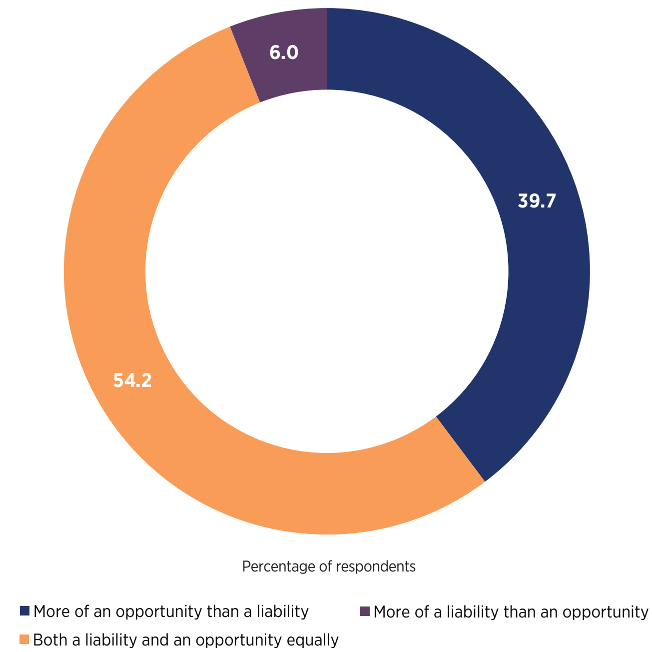


FIGURE 9

How does your bank view future technology innovation in banking?

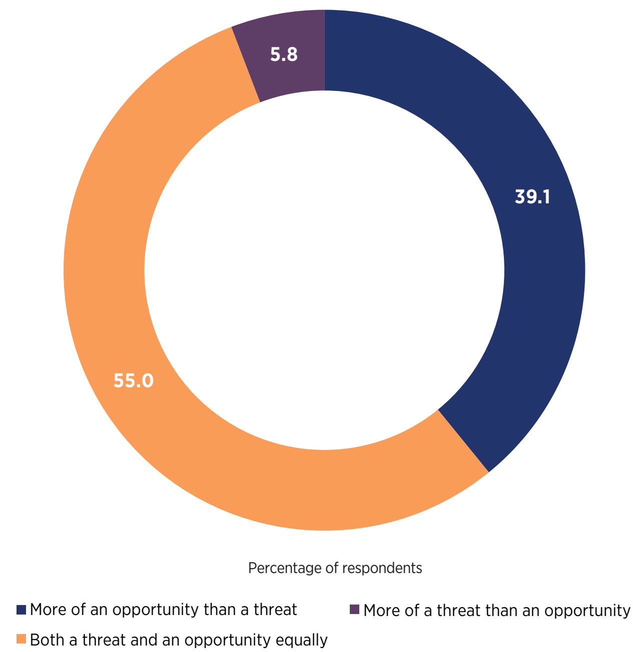
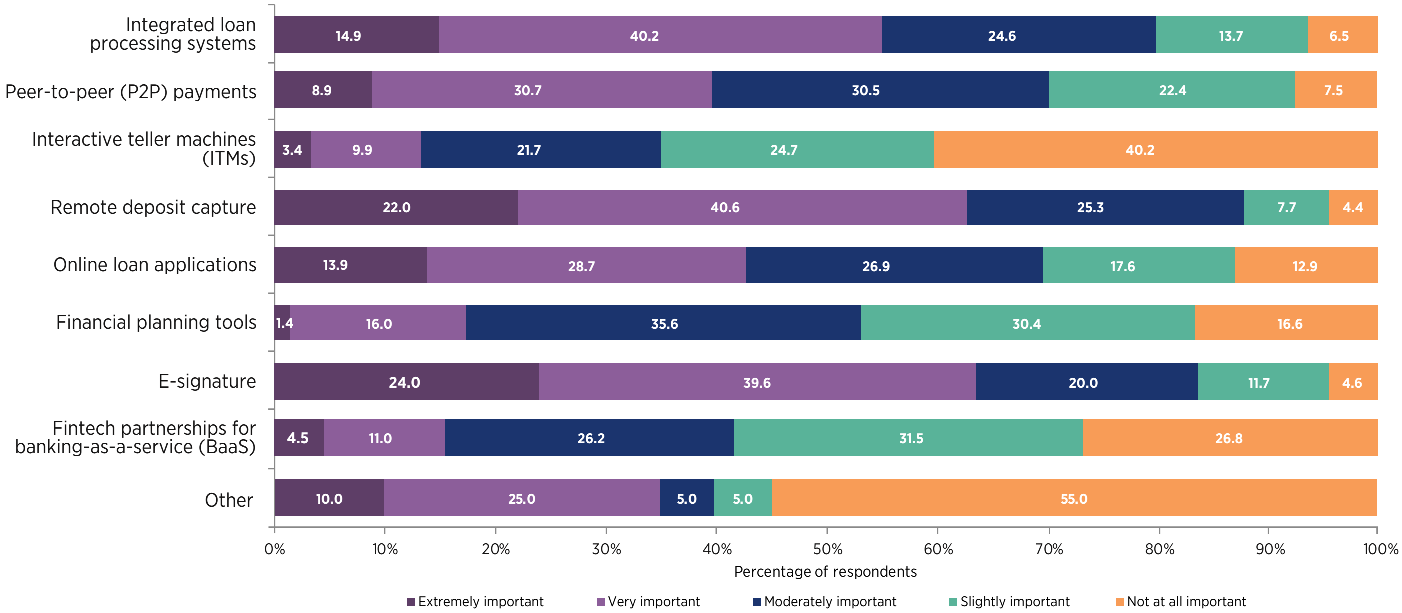


FIGURE 10

How important are the following technologies for your bank?



Additional Technology and Technology Services Findings

- More than 55% of bankers described opportunities in integrated loan processing systems as "extremely important" or "very important." Meanwhile, peer-to-peer payments did not appear to be regarded with the same uniformly high levels of importance.
- About 30% of bankers described online loan applications as less than "moderately important," while 35% of banks neither offered them nor planned to do so. This evidence of lukewarm interest, however, contrasts with the 23% of bankers that did not offer them but planned to do so. Online loan closings and automated loan underwriting were less commonly used.
- About 24% of bankers considered e-signature opportunities to be "extremely important," which is the highest level for any technological service. Half of all banks said they offered e-signature verification, while 22% of bankers planned to introduce it.

FIGURE 11

How important is the adoption of new or emerging technologies to meet customer demand in your market?

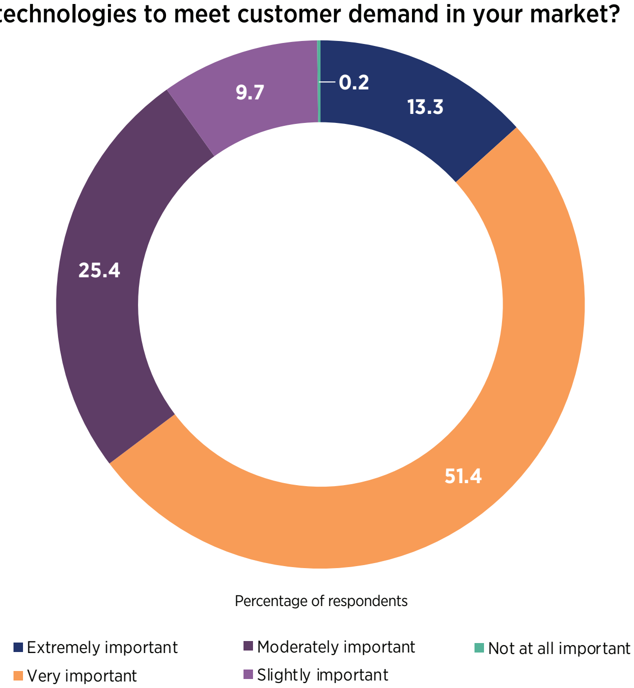
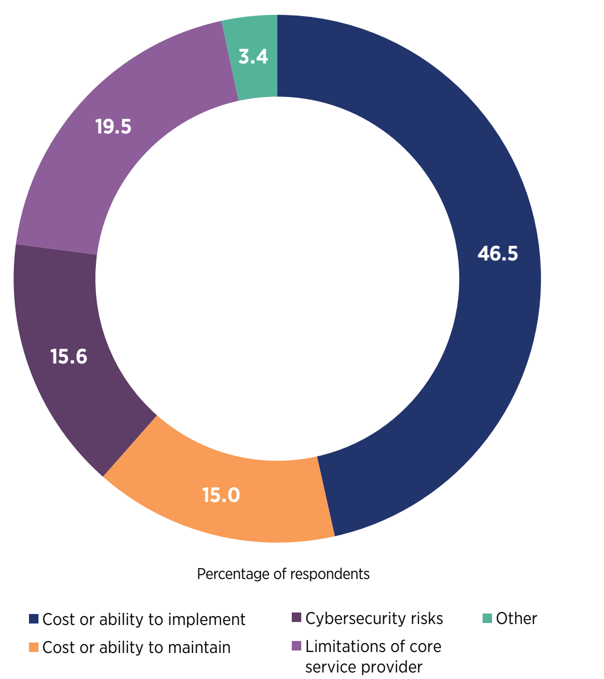


FIGURE 12

What is the most significant impediment to adopting new technologies?



Bankers' Perspectives: Technology Is Now an "And"

If you were to rewind 10 or even 15 years ago, technology was more of an "or" for our customers, not an "and." A lot of banks made the mistake of having technology serve as their primary delivery channel.

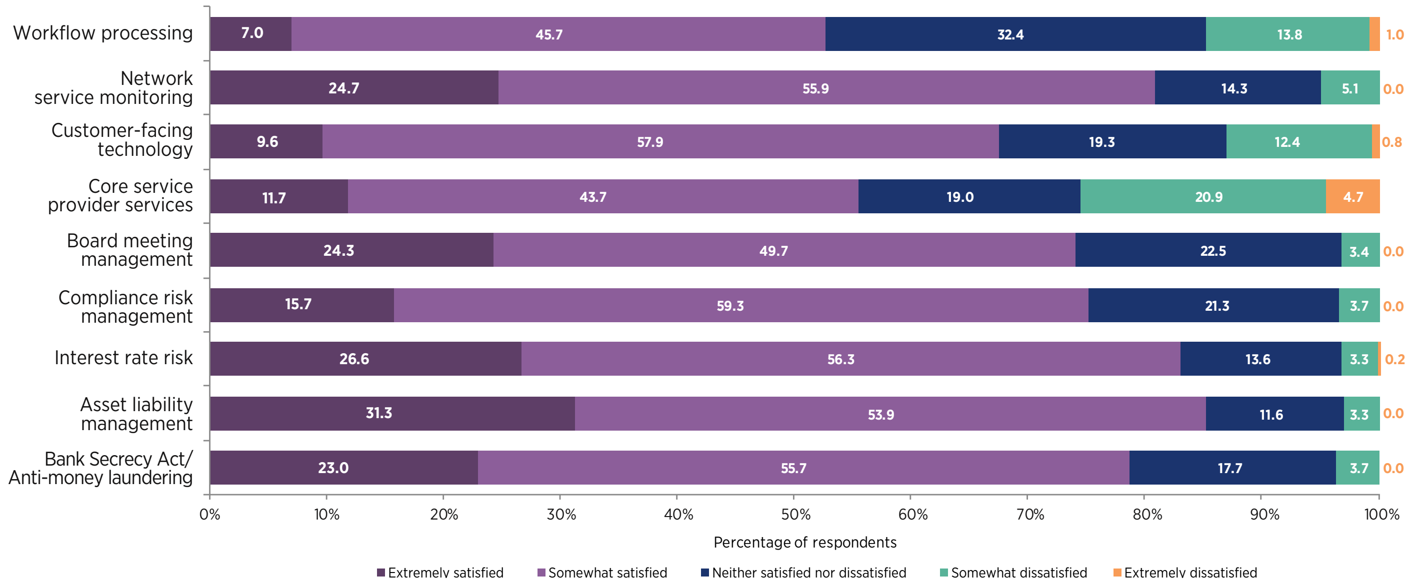
As a community bank, we need to remember our niche and our strengths. Our strength is relationship banking. We should not be afraid of technology that can complement this strength. Technology can expand our horizon on who we can bank.

Today, I can bank customers all over Wyoming and still see them face to face without getting in my car and driving three hours. Technology creates limitless opportunity for us. As long as we can package technology with the relationships that a community bank can offer, we should consider adopting that technology. We need to make technology an "and" option for our customers.

–Kim DeVore, Jonah Bank of Wyoming, Casper, Wyoming

FIGURE 13

How satisfied are you with the effectiveness of your bank's technology in the following areas?



Bankers were most satisfied with the effectiveness of technology in asset liability management. They were most dissatisfied with core service provider services.

FIGURE 14

What technological developments will be promising opportunities for your bank over the next five years?

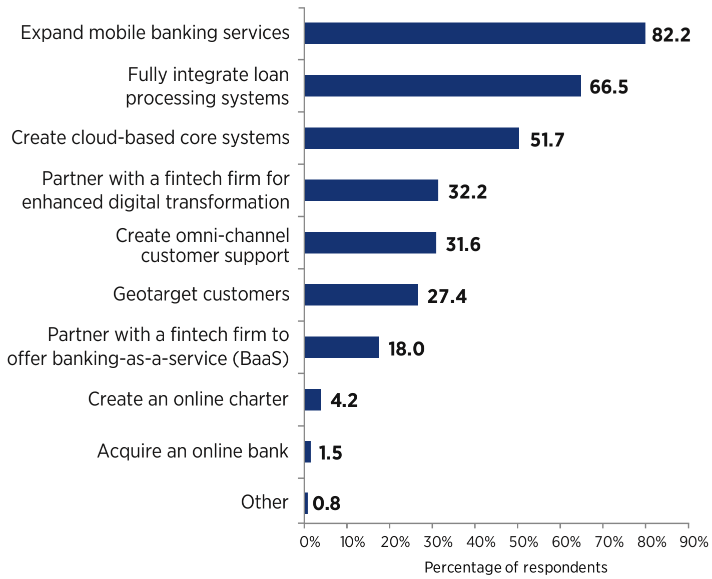


FIGURE 15

What do you see as the most difficult challenges to implementing new technology over the next five years?

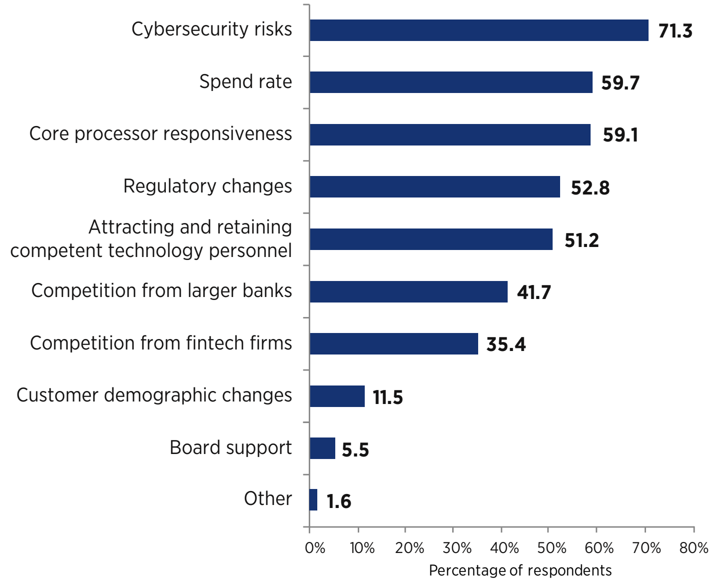
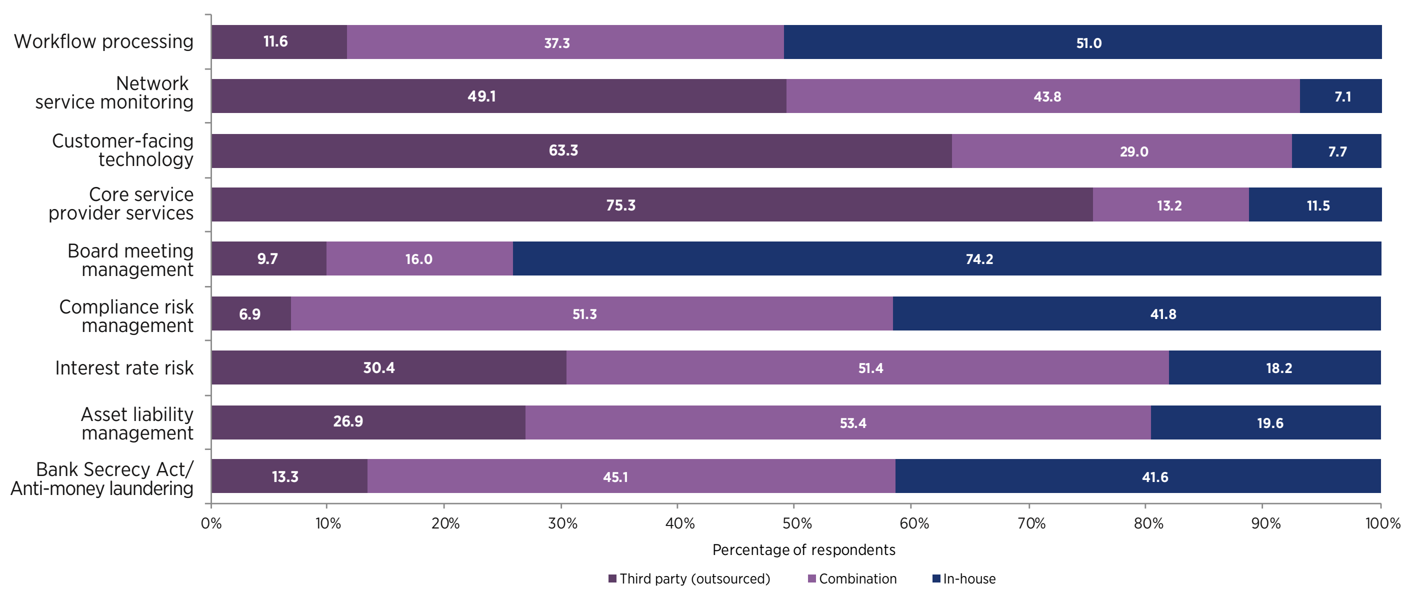


FIGURE 16

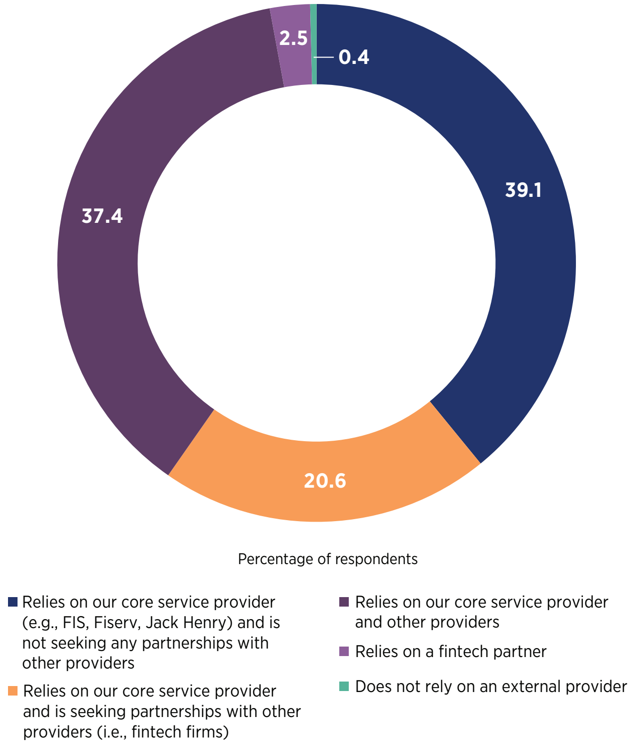
How are your technology needs for the following services being met?



Core service provider services were most likely to be outsourced, while board meeting management and workflow processing were most likely to be done internally. Many services were provided by both.

FIGURE 17

On whom does your bank rely for digital banking products and services?



Core Processing

Core processing systems allow banks to support a variety of services ranging from loan origination to automated clearinghouse transfers. The systems can be provided internally or through external vendors.

FIGURE 18

How satisfied is your bank with in-house core processing services?

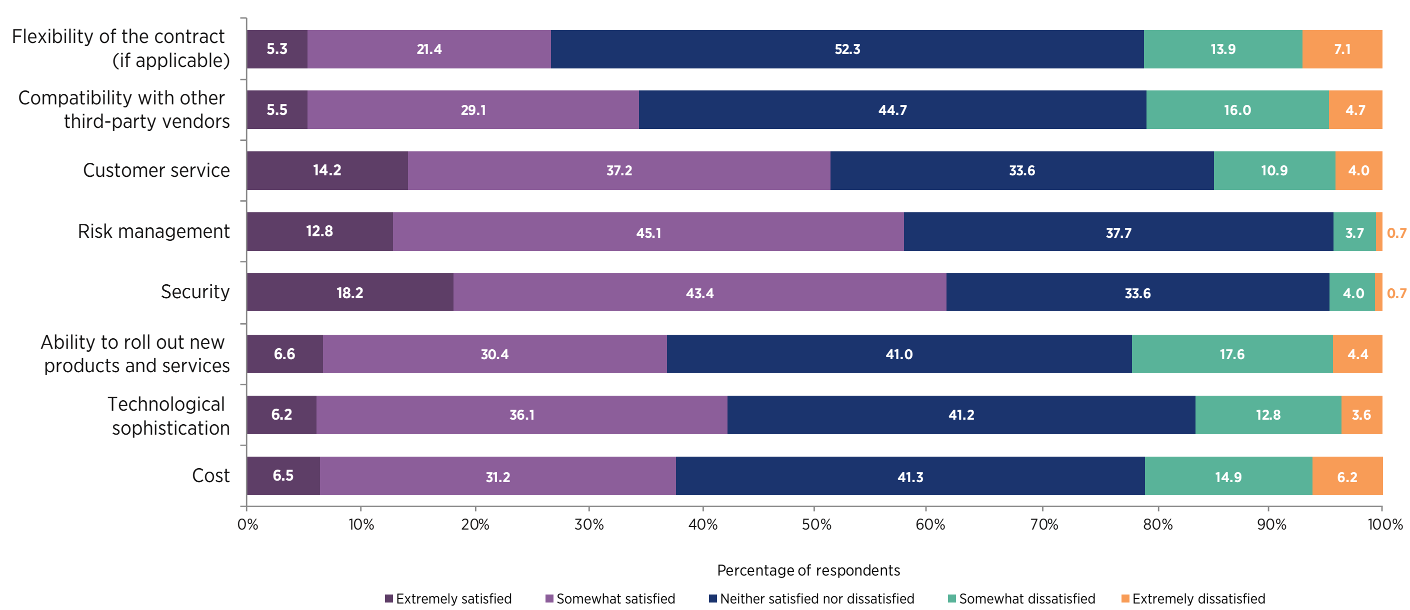
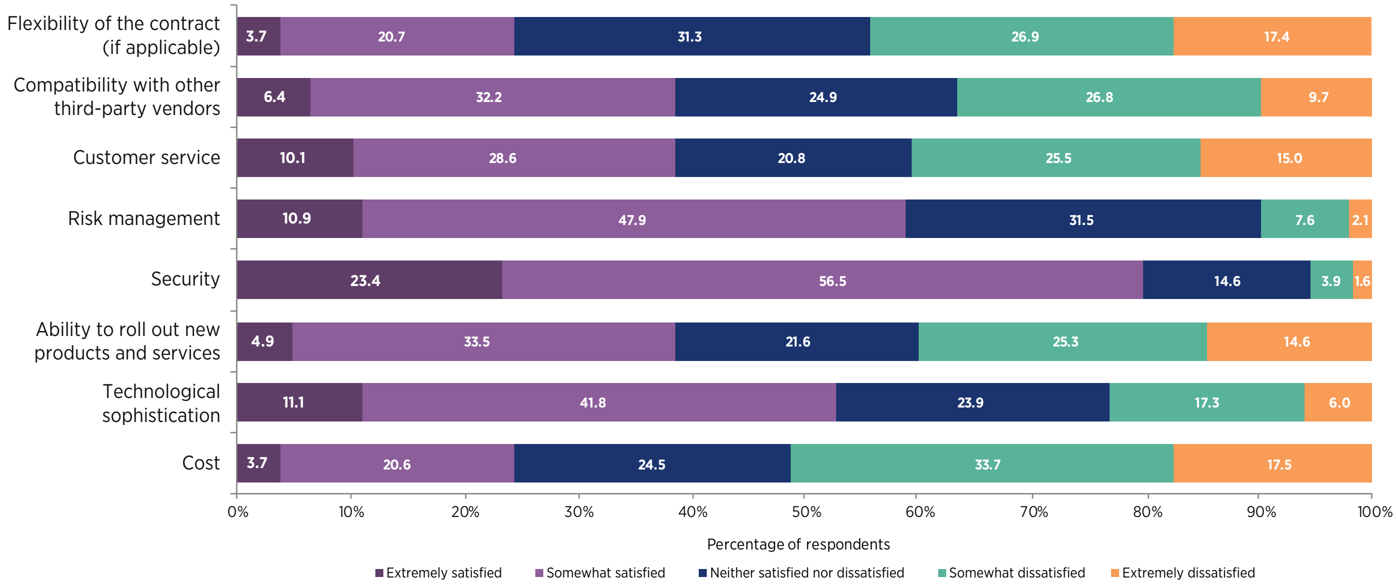


FIGURE 19
How satisfied is your bank with core processing services provided by an external company?



On the Cutting Edge: Crypto and Machine Learning

Cryptocurrency remains a hot topic in the press, but a majority of survey respondents indicate that addressing cryptocurrency needs of customers doesn't present as high importance. Machine learning, natural language processing and other related technologies, on the other hand, do show as important, with 64% of respondents indicating some level of importance.

FIGURE 20
How important is meeting customer cryptocurrency needs at your bank?

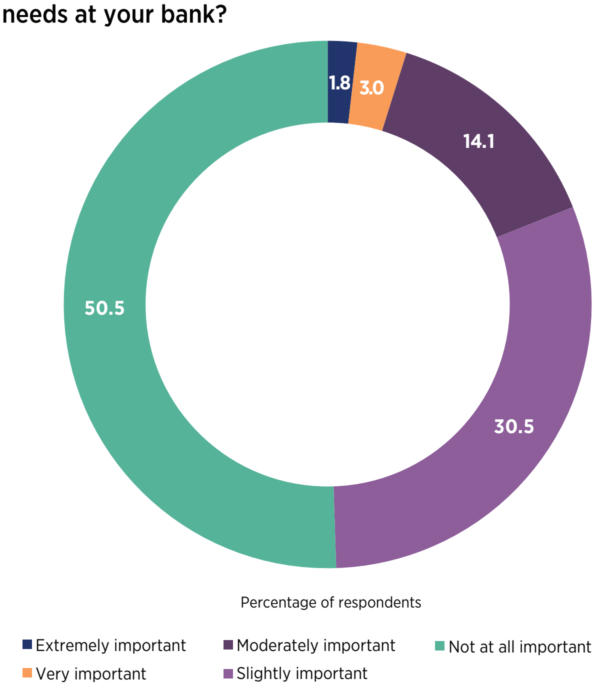
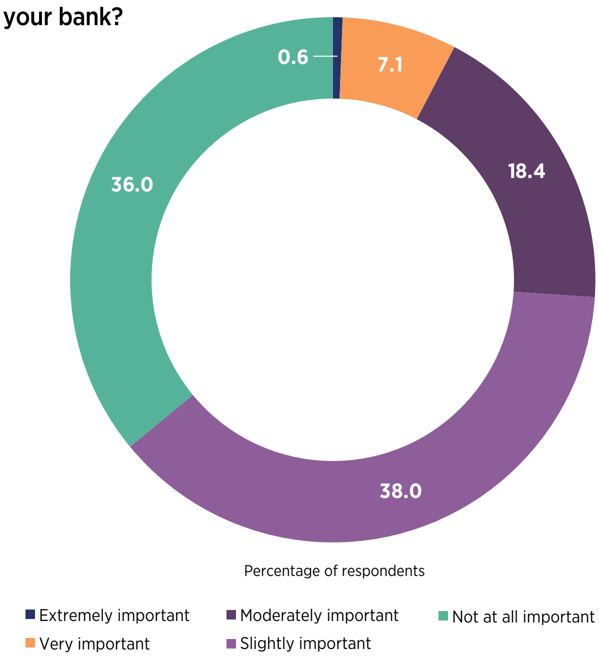


FIGURE 21
How important is the use of machine learning, natural language processing and other related technologies at your bank?

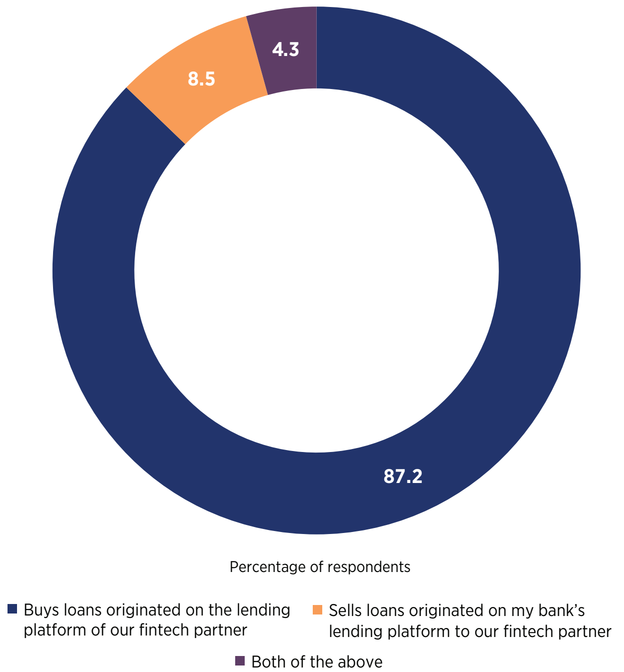


Fintech Partnerships

According to this year's survey, about 10% of banks reported partnering with fintech firms on lending, predominantly for purchases rather than sales. The partnerships mainly involved small-business loans and, to a lesser extent, small-dollar unsecured loans.

FIGURE 22

What does your bank do under a fintech partnership?



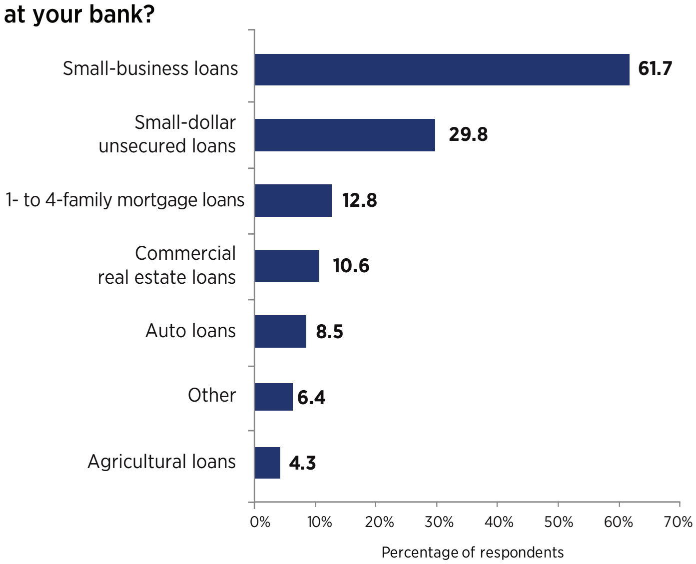
Bankers' Perspectives: Fintech—Friend or Foe?

There is ongoing debate as to whether fintechs should be considered competitors, potential partners or even acquisition targets. I lean toward the middle option, recognizing that we have something they want, in our deep and long-standing customer relationships, and that they have something we want, in their innovative solutions for those customers.

–Rogers Pope Jr., Texas Bank and Trust Co., Longview, Texas

FIGURE 23

What types of loans fall under a fintech partnership at your bank?



Bankers were asked a series of questions, some of them new, concerning sources and intensity of competition. Figures 24 and 25 give the primary and secondary sources, respectively, of competition for various products and services offered by community banks.

Competition for small-business loans was dominated by community banks and regional/national banks, which were named by 56% and 29% of bankers, respectively, as their primary competitors and by 30% and 35% of bankers, respectively, as their secondary competitors. Nonbank, non-credit union institutions without a local presence were named as the primary competitors by 4% of bankers—a level double the 2% reported last year. More than 76% of bankers named other community banks or regional or national banks with a local presence in the market as their primary competitors for transaction deposits. Credit unions were named by more than 25% of bankers as primary competitors for both.

Competition for agricultural loans was from other community banks and nonbank, non-credit union entities with or without a physical presence in the market. The latter two categories combined—which include, presumably, the Farm Credit System—were named by 48% of bankers as their primary competitors.

Competition for commercial real estate lending came mainly from other community banks and national/regional banks. Nonbank, non-credit union entities with or without a physical presence in the market were named as the primary competitor by 5% of bankers.

Bankers' Perspectives: Bigger Banks Drive Down Pricing

When regional or large banks enter our markets, our risk is that they push our pricing down. When they can't compete on relationships, and they can't compete on community involvement, they will naturally compete on price. That's where their strength lies.

–Kim DeVore, Jonah Bank of Wyoming, Casper, Wyoming

FIGURE 24

Who is your primary competitor for the following products and services?

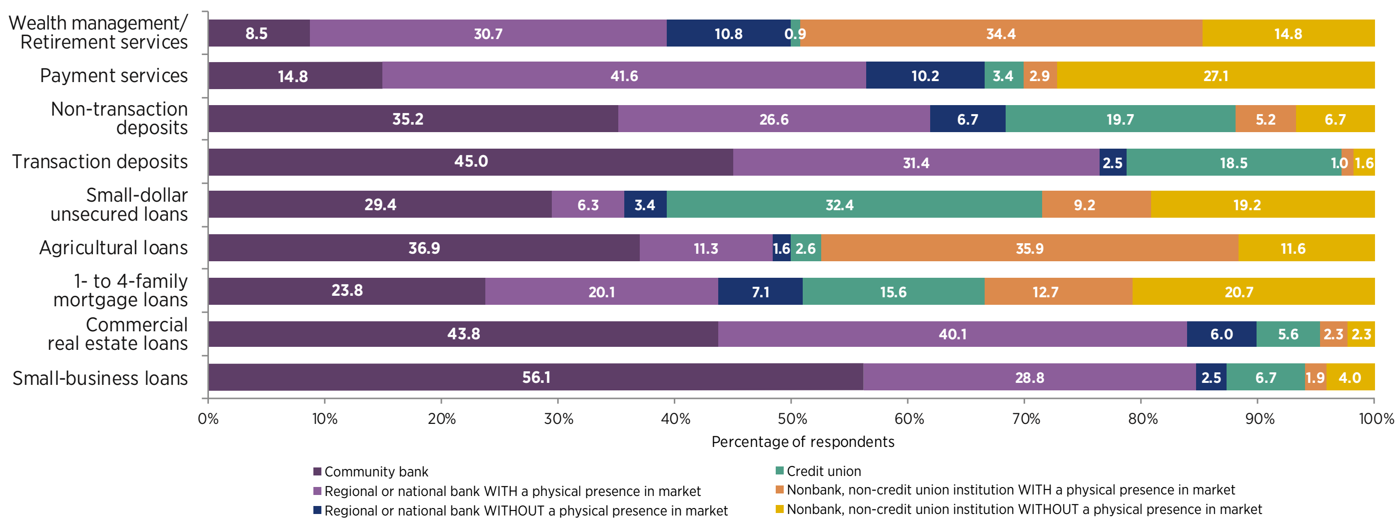


FIGURE 25

Who is your secondary competitor for the following products and services?

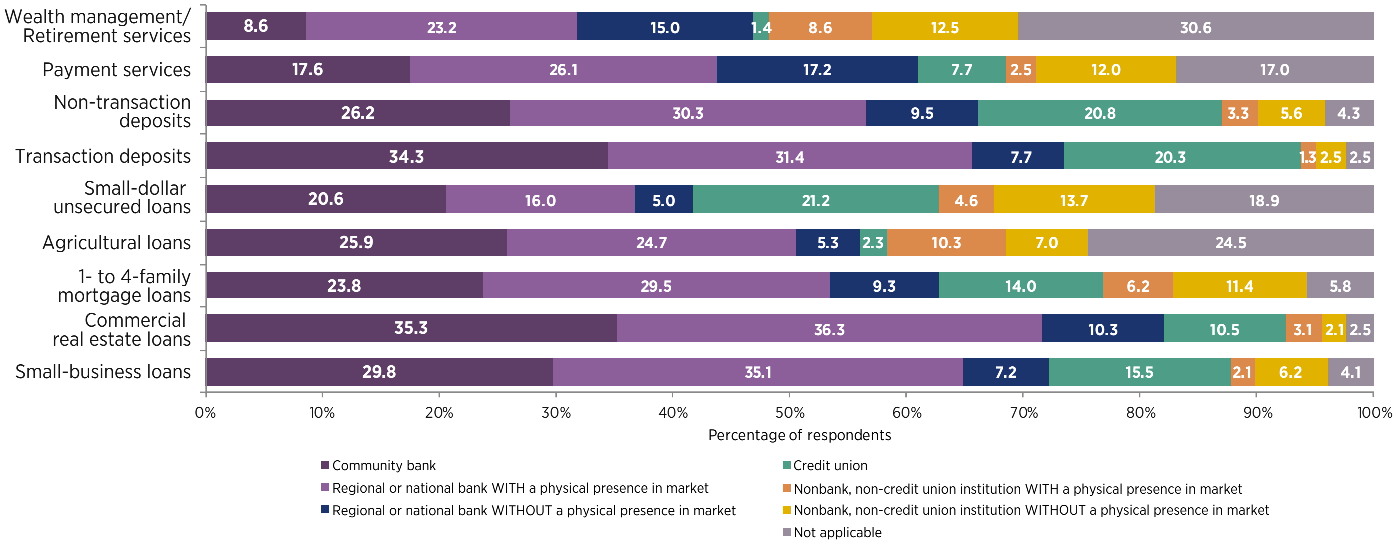


FIGURE 26

How do your bank's pricing decisions on loans and deposits influence local market rates?

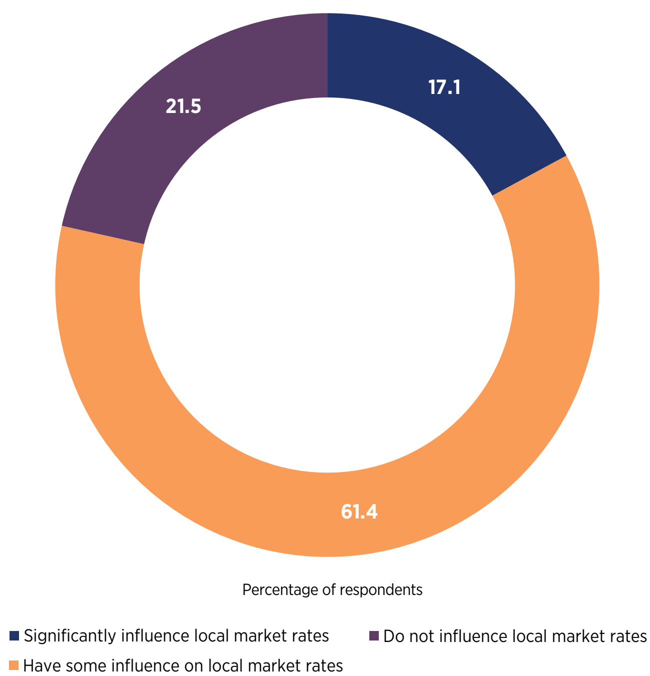


FIGURE 27

How often does your bank respond to changes in local market rates on loans?

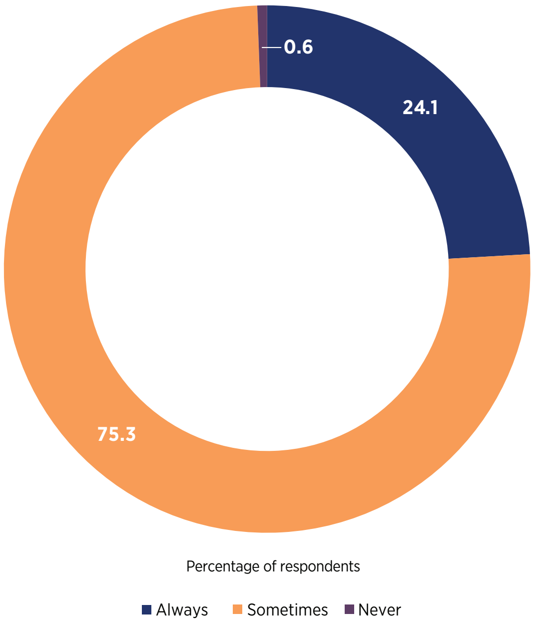
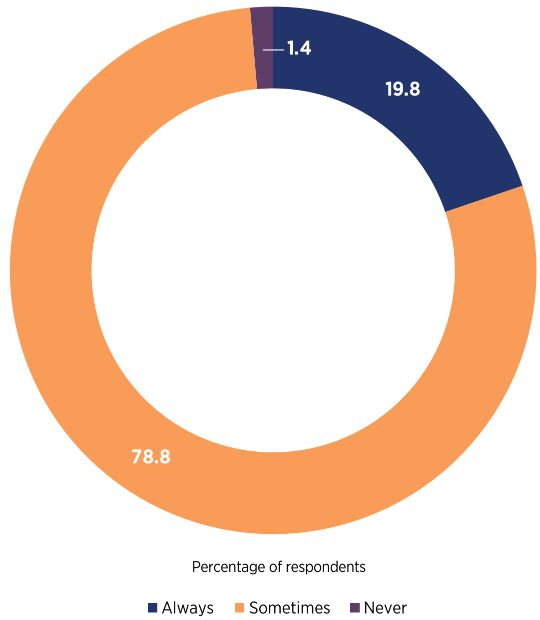


FIGURE 28

How often does your bank respond to changes in local market rates on deposits?



Small-Business Lending

Community bankers have long grappled with a growing tension between their traditional business model of relationship lending and inroads that have been made against it by bigger banks and fintech companies. Percentage changes in levels of small loans to businesses, and ratios of those loans to assets, have been similar across community banks and noncommunity banks (see Table 1).

In 2021, the average loan size for community banks was about three times that of noncommunity banks, compared with about five times just three years earlier (see Table 1). This may be related to an improved ability of community banks to incorporate technology into small-business lending, regardless of loan size.

To be sure, community bankers are optimistic about their business model: As shown in Figure 29, they expect relationship-based lending to grow more than transactional lending.

TABLE 1

Small loans to businesses

	Community banks				Noncommunity banks			
	Dec. 31, 2018	Dec. 31, 2019	Dec. 31, 2020	Dec. 31, 2021	Dec. 31, 2018	Dec. 31, 2019	Dec. 31, 2020	Dec. 31, 2021
Dollar amount	$311.9	$304.7	$384.1	$315.5	$323.2	$340.4	$448.9	$352.1
% of assets	13.7%	13.4%	16.1%	13.3%	4.1%	4.1%	5.3%	4.0%
Number of loans	4,232	4,286	5,845	5,823	21,492	19,308	21,023	20,624
Average loan size	$73.7	$71.1	$65.7	$54.2	$15.0	$17.6	$21.4	$17.1

NOTES: Dollar amounts are in billions of dollars. Numbers of loans are in thousands. Average loan sizes are in thousands of dollars. Data are obtained from Call Reports published by the Federal Financial Institutions Examination Council.

Bankers' Perspectives: High Tech and High Touch

Relationship banking will continue to be a key differentiator among community banks and our chief rivals. … But what constitutes "relationship banking" is a moving target. The rise of the self-directed consumer, and changing behaviors and expectations among borrowers are changing how lending relationships are forged. Going forward, community banks will need to be as much about "high tech" as "high touch."

–Rogers Pope Jr., Texas Bank and Trust Co., Longview, Texas

FIGURE 29

In the future, what do you expect your bank's dollar volume to be on transactional small-business loans compared to relational small-business loans?

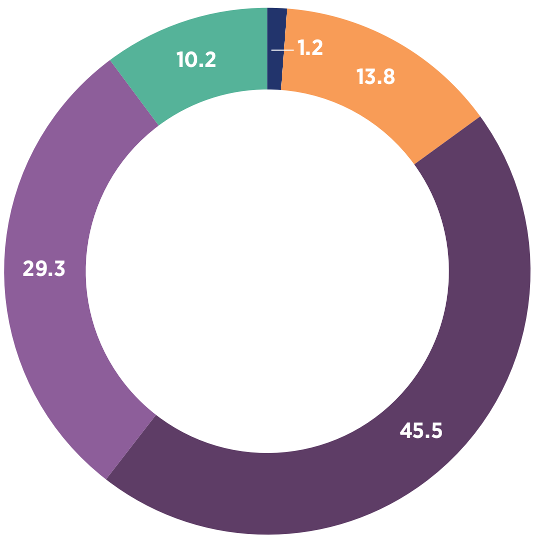
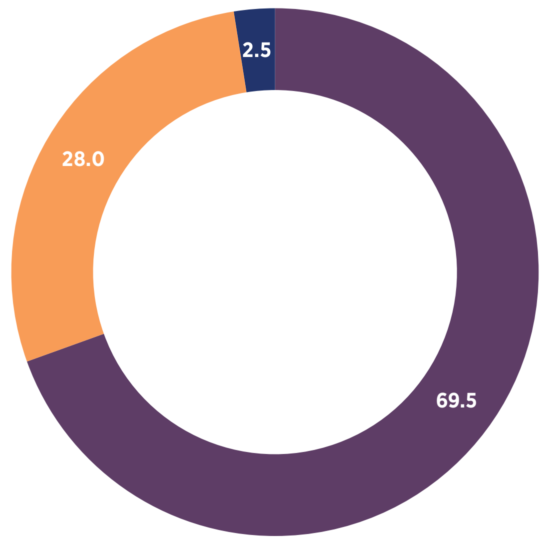


FIGURE 30

At your bank, what is the percentage of small loans to businesses (as defined in the Call Report) that are accounted for by business credit cards?



FUNDING

The liability side of the balance sheets of community banks was transformed by the COVID-19 pandemic, creating problems that still persist. But growth in core deposits leveled off this year (see Table 2), after expanding dramatically in 2020 and 2021. Meanwhile, at least some categories of wholesale funding, which declined in 2021, began to revert upward toward pre-pandemic levels (see Table 3). Some evidence of stability in deposit markets was evident in 2021 following a period of adjustment to pandemic-induced financial shocks. Transaction accounts did not grow, as they did in 2020, and non-transaction accounts did not contract substantially. In the last three years, the percentage of banks with intentions to continue using other borrowed money declined. Banker intentions this year indicated an upcoming reversal, with movement toward pre-pandemic utilization of many wholesale funding sources.

TABLE 2

Core deposits

	Dec. 31, 2019	Dec. 31, 2020	Dec. 31, 2021	March 31, 2022
Transaction	$464.2	$675.0	$910.8	$936.6
Non-transaction	$1,545.3	$1,608.0	$1,565.1	$1,541.8

NOTES: Dollar amounts are collected quarterly for community banks. Data are obtained from Call Reports published by the Federal Financial Institutions Examination Council.

TABLE 3

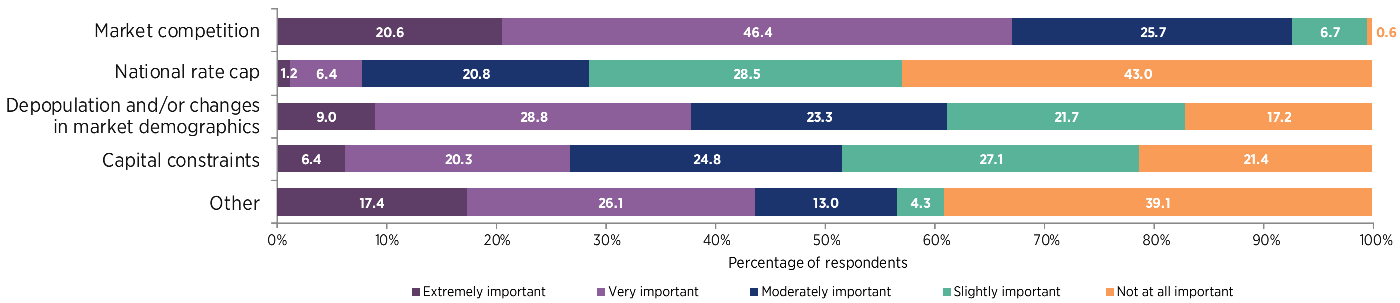
Wholesale funds

	Dec. 31, 2019	Dec. 31, 2020	Dec. 31, 2021	March 31, 2022
Brokered deposits	$110.0	$112.8	$80.5	$85.8
Federal Home Loan Bank advances	$112.3	$87.8	$63.3	$61.8
Other borrowed money (total)	$122.0	$128.4	$82.1	$77.3
Fed funds purchased and repurchase agreements	$5.1	$4.1	$3.4	$4.0
Listing service deposits	$23.9	$23.8	$17.9	$17.4

NOTES: Dollar amounts are collected quarterly for community banks. Data are obtained from Call Reports published by the Federal Financial Institutions Examination Council.

FIGURE 31

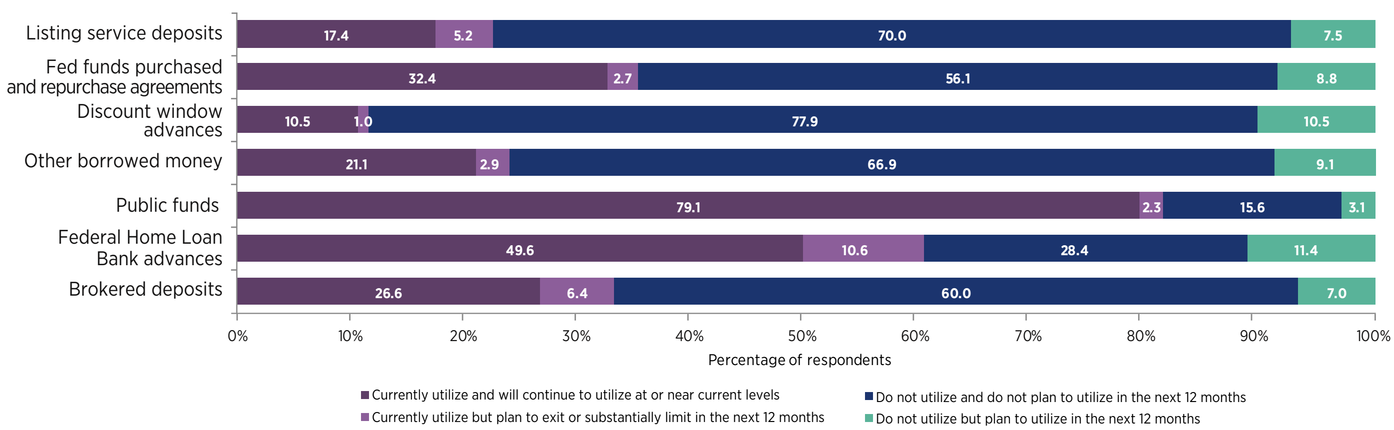
How important are each of the following potential challenges to attracting and retaining core deposits?



Market competition was named by bankers as the most important impediment to retaining core deposits. The national rate cap was considered the least important.

FIGURE 32

What are your bank's intentions regarding the following wholesale funding sources?



Community bankers relied most often on public funds and Federal Home Loan Bank (FHLB) advances as sources of wholesale funds. Discount window advances and listing service deposits were used the least. These rankings on breadth of bank use differ from those on intensity, for which brokered deposits and FHLB advances were greatest (see Table 3).

Perspectives from the Past: Wholesale Funding Declines

From 2014 to 2018, banker responses to questions on their utilization of wholesale funds indicated stability across most categories. Brokered deposits, listing service deposits and FHLB advances were essentially unchanged. Only modest increases were observed in fed funds purchased and public funds. Accelerated expansion of the latter two funding sources was suggested in 2019 by the 11% of community bankers who said they planned to increase utilization of them.

But the pandemic and the economic turmoil of 2022 intervened. The use of wholesale funds declined substantially, rather than increased, across all funding categories. From 2019 to 2022, the percentage of banks using other borrowed money declined from 30% to 21%.

Bankers' Perspectives: Liquidity Problems Will Persist

Ballooning balance sheets have put unexpected stress on capital ratios. We need to deploy the excess liquidity. While loan demand has picked up, it is not enough to make a significant dent in the amount of excess cash we are holding. We can take advantage of investment yields, which have gone up significantly, and we are looking at expanding loan products and services, but it may take us a while to start producing a pre-pandemic return on assets.

–Janet Silveria, Community Bank of Santa Maria,
Santa Maria, California

LOAN PARTICIPATIONS

FIGURE 33

What percentage of loans sold at your bank are loan participations?

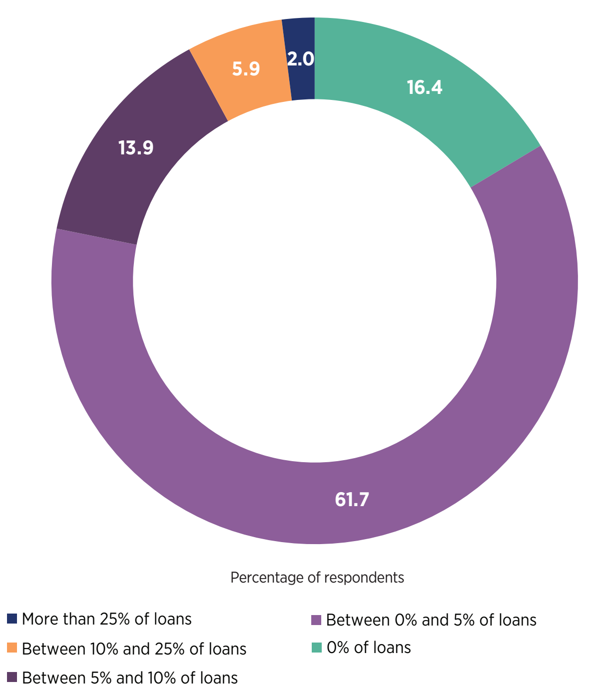


FIGURE 34

What is the primary reason loan participations are sold at your bank?

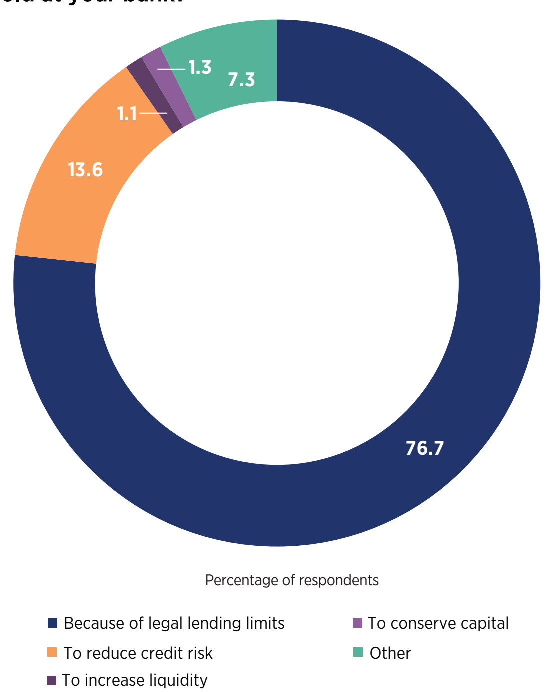


FIGURE 35

What percentage of loans purchased at your bank are loan participations?

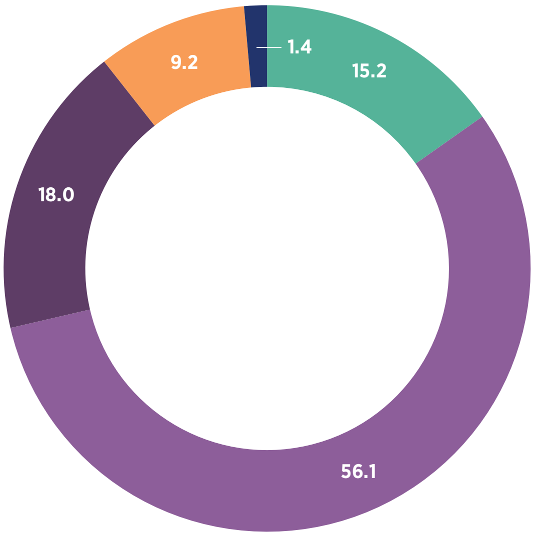
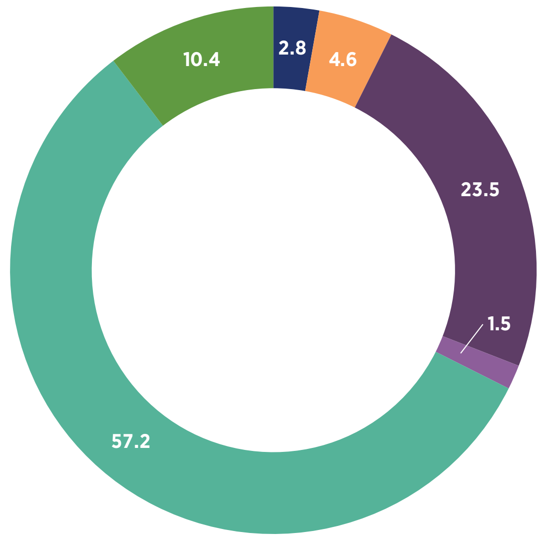


FIGURE 36

What is the primary reason loan participations are purchased at your bank?



REGULATORY COMPLIANCE

Costs incurred by banks to comply with regulations may be high, from the perspective of community bankers, but appear to be stabilizing, after sharp increases were reported in surveys from earlier years of the conference. This year, for instance, compliance accounted for 10% of total personnel expenses—an amount that reflects what was reported in each of the last four years (see Table 4). Similar results were reported in the other expense categories of data processing, legal, accounting and auditing, and consulting and advisory. Although personnel, by far, was the largest expense category in terms of dollar volume, other categories had higher ratios of compliance expense to total expense.

TABLE 4

Compliance costs as a percentage of total expenses by category

	Dec. 31, 2017	Dec. 31, 2018	Dec. 31, 2019	Dec. 31, 2020	Dec. 31, 2021
Personnel (salary and benefits)	**10.4** *(7.1)*	**11.3** *(6.4)*	**10.3** *(5.8)*	**9.8** *(5.2)*	**10.3** *(6.9)*
Data processing	**17.1** *(12.4)*	**18.0** *(12.6)*	**17.1** *(11.0)*	**17.1** *(12.1)*	**17.6** *(14.0)*
Legal	**20.9** *(12.5)*	**22.8** *(14.5)*	**22.6** *(14.3)*	**22.6** *(15.4)*	**26.8** *(20.2)*
Accounting and auditing	**39.4** *(32.3)*	**42.4** *(35.3)*	**42.3** *(36.5)*	**42.8** *(37.2)*	**39.5** *(33.8)*
Consulting and advisory	**45.9** *(41.7)*	**40.5** *(34.4)*	**38.2** *(28.2)*	**41.8** *(33.3)*	**36.1** *(30.7)*

NOTE: The percentages are means (first rows) and medians (second rows) of ratios of compliance costs to total expenses within a given expense category.

In the first years of the conference, regulatory burden was a dominant concern, spurred by implementation of Dodd-Frank. In 2015, more than 10% of community bankers said compliance costs had increased by more than 90% in the previous three years, and 95% of them cited increases of at least 10%. Median compliance expenses for personnel—by far the largest expense category—then represented 7.5% of total personnel expenses, increasing slightly to 7.7% in 2016.

But the tide turned in 2017, perhaps influenced by the Economic Growth and Regulatory Paperwork Reduction Act of 1996, which reduced financial reporting requirements and lengthened examination cycles, and expanded differentiated regulatory technologies (RegTech), which are increasingly used to drive efficiencies in compliance processes through automation, advanced analytics and cognitive computing. Median personnel costs related to regulatory compliance as a percentage of total personnel expenses dropped to 7.1% in 2017 and has remained below that level since. These data confirm expectations of more than half of bankers in 2017 that regulatory burden would remain the same in the future.

SPECIAL QUESTIONS

Two topics were the subjects of special questions this year: The first topic was about the current expected credit losses (CECL) methodology, while the second topic was about COVID-19 guidance.

FIGURE 37

What is your bank’s planned date for transitioning to current expected credit losses (CECL) methodology?

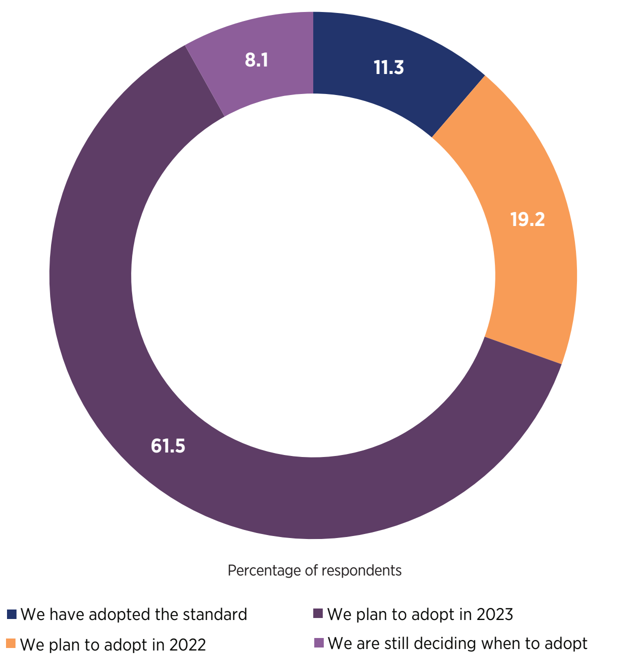
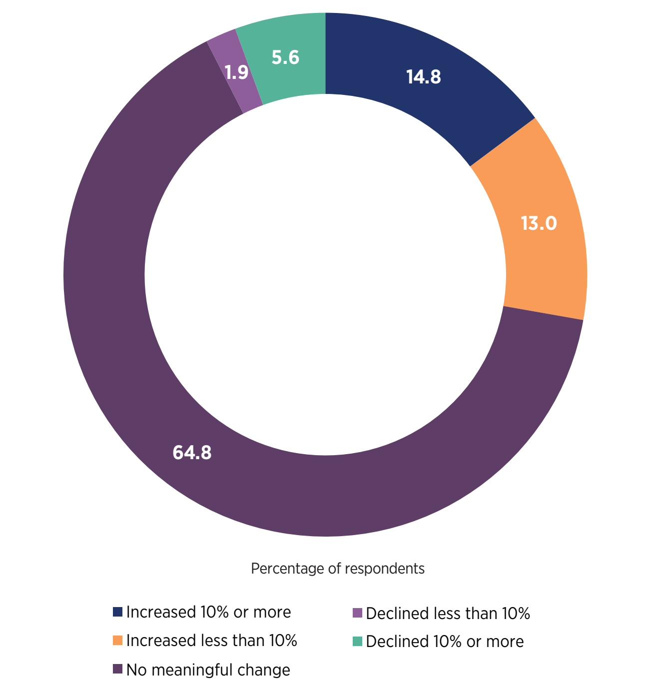


FIGURE 38

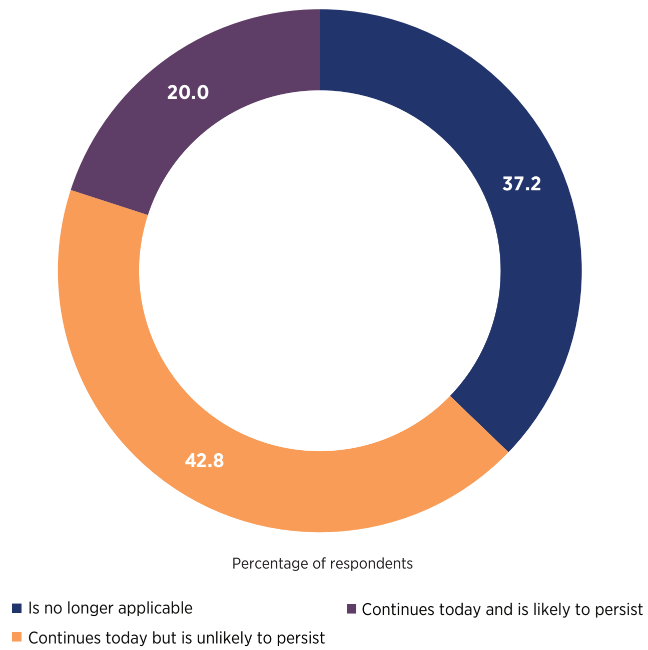
What impact did the adoption of current expected credit losses (CECL) have on your bank's level of reserves in 2021?



Adoption of the CECL methodology: Community bankers are not rushing to convert to the CECL model; more than 61% of them are planning to defer implementation to 2023. Of those that have already implemented CECL, about 28% said reserves for loan losses increased to some extent as a result, compared with 60% last year.

FIGURE 39

What is the status of the guidance to "promote consistency and flexibility" in supervision introduced during the COVID-19 crisis?



COVID-19 guidance: About 37% of bankers said guidance to promote consistency and flexibility during the COVID-19 crisis was no longer applicable, while nearly 20% expected it to persist.

ACQUISITION ACTIVITY

Consolidation has characterized community banking for decades. But activity has trended down in recent years. Indeed, percentages of banks considering, or making, acquisition offers declined this year. About 11% of surveyed bankers said they had made a bid to acquire another institution, while 8% said they had considered an acquisition offer. In comparison, last year's levels were 12% and 7%, respectively. About 38% of bankers said succession issues were "extremely important" in their consideration of accepting acquisition offers. Achieving economies of scale was named by nearly 38% of bankers as "extremely important" in considering acquisition offers and by 38% of those making acquisition bids. Last year, the levels were 24% and 47%, respectively.

FIGURE 40

How important were the following motivations to make the offer?

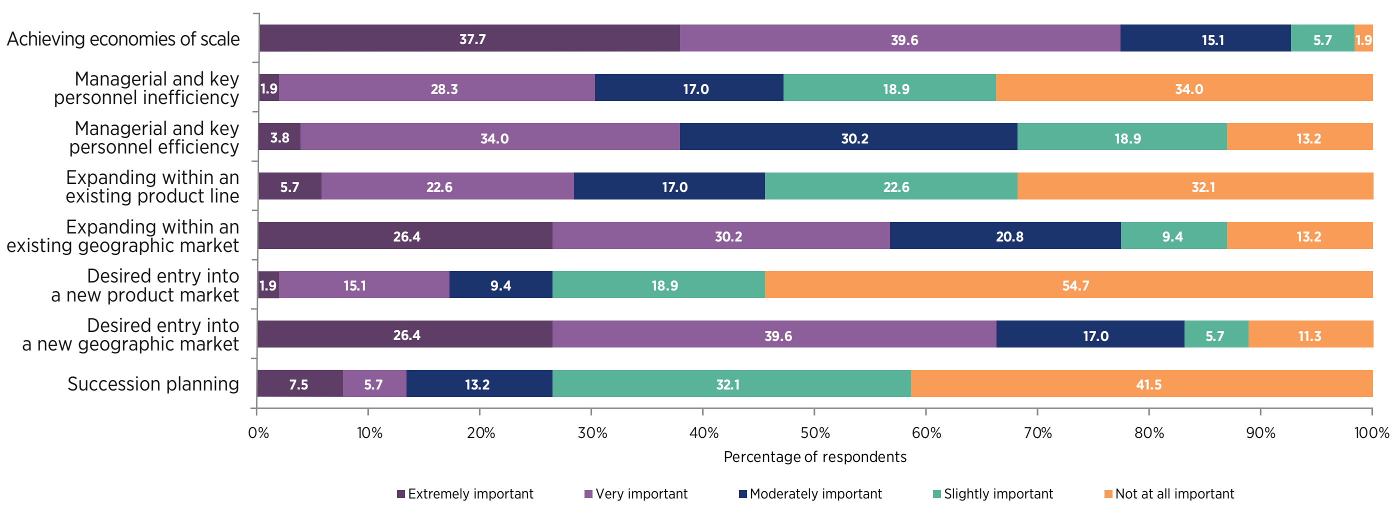
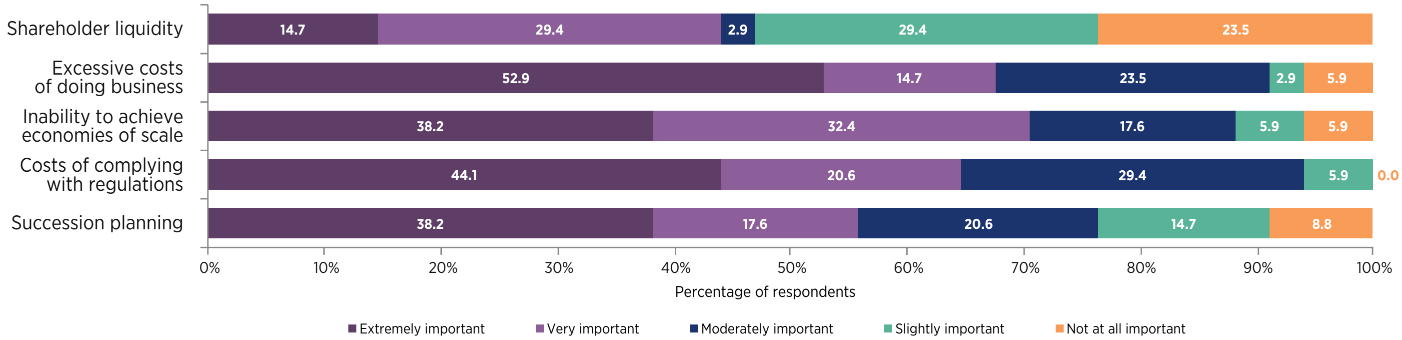


FIGURE 41

How important were the following factors in your decision to seriously consider accepting the acquisition or merger offer?



Perspectives from the Past: Pressures to Achieve Scale Persist

The banking industry has been consolidating over the years, with the number of community banks dropping steadily from 6,416 in 2013 to 4,353 in 2022. Consolidation has resulted not only in fewer banks but in greater size among those that survive. In the 2014 survey, 80% of banks had assets under $300 million; this year, 51% did.

This year, 38% of bankers said the inability to achieve economies of scale was an "extremely important" factor in their consideration of acquisition offers, up from 33% recorded in 2017. Similarly, 38% of bankers said economies of scale were "extremely important" considerations in their acquisition bids.

Bankers' Perspectives: Consolidation Threatens Viability

The continued consolidation of our industry is disheartening. Increasing technology and regulatory obstacles, together with other challenges such as talent recruitment and retention, will make it harder for smaller community banks to maintain an acceptable level of profitability while striving to adequately meet the banking needs of their communities. It is incumbent upon bankers, regulators and third-party financial service providers to find a way to reverse this trend and ensure the long-term viability of the community banking industry.

–Rogers Pope Jr., Texas Bank and Trust Co., Longview, Texas

CONCLUSION

Over the last nine years of the survey, community bankers have answered an evolving array of questions. Their responses have been conditioned by factors such as technological transformation, changes in regulatory guidelines and the COVID-19 pandemic. The prism this year was macroeconomic: Overall, net interest margins ranked first in importance among external risks. Of lesser concern were inflation, which was described as manageable, and higher interest rates, which failed to exacerbate concerns with net interest margins.

Among other findings, cybersecurity ranked first in importance among internal risks, as well as in current and future technological challenges. Despite ongoing declines in small-business lending, community bankers expect relationship-based lending to expand more than transactional lending. At the same time, community bankers continue to place a high value on adopting new technology. Community bankers worried less about competitive risks than they did a year ago, although nonbank, non-credit union institutions without a local presence were a factor in some lending categories.

These findings, along with the findings of previous surveys, underscore the agenda outlined by the late John Ryan, former CSBS president and CEO, at the first conference: to "strive for better tools to assess how our banking system is meeting the diverse needs of our economy and whether we are achieving our goals of a more stable and resilient financial system." These reports over the years can be seen as working toward the goal for the conference set out by then Federal Reserve governor and now Chair Jerome Powell at its inception: "to inform discussions among policymakers, to collect unique and innovative practices of successful community banks and to serve as a reference point for future research conferences."

ACKNOWLEDGMENTS

The 2022 CSBS National Survey of Community Banks was administered by state bank commissioners in 40 states. A total of 498 community bankers participated.

Participation in the 2022 survey would not have been possible without the efforts of the following state bank commissioners and their staffs:

Alabama

Mike Hill, Superintendent
Alabama State Banking Department

Arizona

Evan G. Daniels, Director
Arizona Department of Insurance
and Financial Institutions

Arkansas

Susannah Marshall, Bank Commissioner
Arkansas State Bank Department

California

Clothilde (Cloey) V. Hewlett, Commissioner
California Department of Financial Protection
and Innovation

Colorado

Ken Boldt, State Bank Commissioner
Colorado Division of Banking

Connecticut

Jorge Perez, Banking Commissioner
Connecticut Department of Banking

Georgia

Kevin B. Hagler, Commissioner
Georgia Department of Banking and Finance

Hawaii

Iris Ikeda, Commissioner
Hawaii Division of Financial Institutions Department of Commerce and Consumer Affairs

Illinois

Mario Treto Jr., Secretary
Illinois Department of Financial
and Professional Regulation

Indiana

Tom Fite, Director
Indiana Department of Financial Institutions

Iowa

Jeff Plagge, Superintendent
Iowa Division of Banking

Kansas

David Herndon, Commissioner
Kansas Office of the State Bank Commissioner

Kentucky

Charles Vice, Commissioner
Kentucky Department of Financial Institutions

Louisiana

Stanley M. Dameron, Commissioner
Louisiana Office of Financial Institutions

Maryland

Antonio Salazar, Commissioner
Maryland Office of Financial Regulation

Massachusetts

Mary Gallagher, Commissioner of Banks
Massachusetts Division of Banks

Michigan

Anita Fox, Director
Michigan Department of Insurance
and Financial Services

Minnesota

Grace Arnold, Commissioner
Minnesota Department of Commerce

Mississippi

Rhoshunda Kelly, Commissioner
Mississippi Department of Banking and
Consumer Finance

Missouri

Mick Campbell, Acting Commissioner
Missouri Division of Finance

Montana

Melanie G. Hall, Commissioner
Montana Division of Banking
and Financial Institutions

Nebraska

Kelly Lammers, Director
Nebraska Department of Banking and Finance

Nevada

Sandy O'Laughlin, Commissioner
Nevada Financial Institutions Division

New Mexico

Mark Sadowski, Director
New Mexico Financial Institutions Division

New York

Adrienne A. Harris, Superintendent
New York State Department of Financial Services

North Carolina

Katherine M.R. Bosken, Commissioner
North Carolina Office of the Commissioner of Banks

North Dakota

Lise Kruse, Commissioner
North Dakota Department of Financial Institutions

Ohio

Kevin Allard, Superintendent
Ohio Division of Financial Institutions

Oregon

TK Keen, Administrator
Oregon Division of Financial Regulation

Pennsylvania

Richard Vague, Secretary
Pennsylvania Department of Banking and Securities

South Carolina

Kathy L. Bickham, Commissioner of Banking
South Carolina Board of Financial Institutions

South Dakota

Bret Afdahl, Director
South Dakota Division of Banking

Tennessee

Greg Gonzales, Commissioner
Tennessee Department of Financial Institutions

Texas

Charles G. Cooper, Commissioner
Texas Department of Banking

Utah

Darryle Rude, Interim Commissioner
Utah Department of Financial Institutions

Virginia

Joe Face, Commissioner
Virginia Bureau of Financial Institutions

Washington

Charles E. Clark, Director
Washington State Department
of Financial Institutions

West Virginia

Dawn E. Holstein, Commissioner
West Virginia Division of Financial Institutions

Wisconsin

Cheryll Olson-Collins, Secretary-designee
Wisconsin Department of Financial Institutions

Wyoming

Jeremiah Bishop, Banking Commissioner
Wyoming Division of Banking

Janet Silveria

Janet Silveria is president and CEO of the Community Bank of Santa Maria, Santa Maria, California. Silveria joined the bank, which has $411 million in assets, as chief financial officer when it opened more than 20 years ago. She has been active in many civic and professional organizations, including serving as chair of the Community Depository Institutions Advisory Council of the Federal Reserve Bank of San Francisco. Community Bank specializes in small-business lending.

Current Risks

The top three risks at my institution are finding talented lenders, managing excess liquidity and combating fraud and cybersecurity.

In terms of talent, we are trying to figure out how to effectively develop our own lenders. Historically, community banks were successful at recruiting them away from larger banks. But as larger banks have become more "siloed" in their loan processes, it has been increasingly challenging to locate bankers with the well-rounded knowledge of "cradle-to-grave" lending that is vital to relationship banking. We are taking steps to keep the relationship model alive and well using the workforce available to us. We are adapting our loan processes to meet the skill set of the labor pool and are developing additional skills internally with the use of various training programs.

The risk related to managing excess liquidity comes down to managing capital. Ballooning balance sheets have put unexpected stress on capital ratios. We need to deploy the excess liquidity. While loan demand has picked up, it is not enough to make a significant dent in the amount of excess cash we are holding. We can take advantage of investment yields, which have gone up significantly, and we are looking at expanding loan products and services, but it may take us a while to start producing a pre-pandemic return on assets. Continued patience by regulators would be greatly appreciated. Risks have not increased, and credit quality is strong, so growing capital is strictly a matter of getting earnings to keep pace with asset growth.

The third risk extends from the growing resources required to combat fraud and manage cybersecurity. Check fraud is on the rise. With the check-clearing process now completely automated, forged checks are slipping through; protective software programs are difficult to adopt because of high costs and required participation of customers. Debit card fraud takes staff resources to manage, while detection and insurance programs, once again, are costly. Combating wire fraud and other transactional scams requires staff and customer education. And when it comes to cybersecurity, it takes considerable time to keep up with changing threats and regulatory expectations. We are typically in a reactive mode. We really don't have the time or expertise to stay ahead of fraud criminals.

On a macro level, there are numerous threats to community banks: increased regulatory burden, increased reach of credit unions, the economy and rising inflation.

Competition

We have noted an increase in competition from online mortgage and small-business lenders. We compete with traditional products but try to be flexible by tailoring them to meet customer needs. For many customers, especially small businesses, creative financing is required to obtain credit; they simply cannot obtain "outside-the-box" loans from larger institutions that are rigid in their qualification and structure standards.

It is noteworthy to mention that flexibility with credit qualification and structure is difficult when it comes to consumers. Regulations do not allow for flexibility. This results in fewer consumers being able to obtain the credit they need.

Continued consolidation will increase the need for true community banks that know and understand their customers and the communities in which they are doing business.

Technology

As primarily a small-business bank, we are focused on technology that improves efficiency but does not necessarily keep up with consumer driven e-delivery channels. We do have the basic modern conveniences for consumers (automated teller machines, online banking, bill pay, mobile deposit), but going beyond that to adopt emerging technologies (budgeting apps, interactive teller machines, bio authentication) is outside our reach. For businesses, we have business cash management and remote deposit capture.

Community banks, in general, are limited by an ability to adopt emerging technologies due to a reliance on core providers.

Relationship Lending

I cannot envision a world where relationship banking becomes irrelevant. There are so many benefits, and there are so many people who would lose access to credit. Fintechs and large banks operate in a box and determine the character of borrowers based strictly on their credit scores. Community banks are nimble and flexible and determine character based on a plethora of knowledge about borrowers, their histories, their customers, the communities they do business in, etc. We have greater knowledge and understanding of collateral. We don't wait for the borrowers to become delinquent. We get ahead of that. And in the event a credit becomes a problem, we are better positioned to help the borrowers work their way out of it.

So how do we quantify it? We quantify it by our ability to avoid losses. And we quantify by the number of small businesses we serve that have been turned away by other institutions—no loan is too small for us, and every customer receives the same level of responsiveness and support.

Underserved Communities

Reaching underserved communities is different for every bank. I would define ours as migrant and immigrant agricultural workers. But we cannot make them come to us. All we can do is make our best effort at ensuring that we are accessible to them. Barriers of language, mistrust and lack of financial literacy are obstacles to overcome.

We are extremely active in our efforts to get the entire community to recognize our commitment to serving every person. There is not an event or a fundraiser that takes place that we don't have staff present. We work with our customers to ensure that costs for service charges, overdraft fees and other services are not a deterrent to maintaining a banking relationship with us. We offer loans to students in Future Farmers of America and 4-H to help ensure that no child is prohibited from participating in these valuable learning activities due to lack of financial support.

One thing I know for sure about the Community Reinvestment Act: Credit unions, online banks and fintechs should be held accountable to the same standards as commercial banks.

Pandemic Impacts

The pandemic solidified our business model. People were abandoned by larger banks that closed branches, had staff working remotely and offered no way for customers to get support. We extended hours when others closed, continued to have a live person answering our phones and always had a portion of our staff on-site. In other words, we maintained our focus on "being there" for our customers.

The pandemic did force us to innovate very quickly, which we were not accustomed to doing. We expedited the launch of mobile deposit and e-signature services and learned how to navigate virtual meetings very quickly. Ultimately, we discovered that on-site staff is crucial to preserve our culture, but those innovations are still heavily utilized and appreciated.

We are extremely complimentary of the way the regulatory agencies supported us and provided the opportunity to work with our borrowers. That was a complete 180-degree turnaround from the Great Recession when we were pressured to recognize losses.

Rogers Pope Jr.

Rogers Pope Jr. is CEO and vice chairman of Texas Bank and Trust Co. in Longview, Texas. In this capacity, Pope assists with the overall management of the bank and its holding companies. An attorney specializing in banking law, Pope was employed in the financial institutions practice group of the Dallas law firm of Gardere Wynne Sewell LLP prior to joining Texas Bank and Trust.

Current Risks

First, operational risks. We continue to experience more incidents of fraud, primarily via the use of technology, and this risk continues to grow—whether it comes from increasingly sophisticated “bad actors” who are developing more tools through which to inflict damage or simply from an expansion of digital banking channels that creates more vulnerability. Defending against fraud is a never-ending battle. We are well aware that one simple misstep by one of our own team members, or by a customer, could have significant adverse consequences.

Second, regulatory risks are frustrating in that we are subject to a pendulum that swings back and forth based upon changes in the current administration, creating seemingly constant changes in the application and/or interpretation of regulations. Currently, of course, the pendulum seems to lean toward increased regulation, which affects smaller community banks disproportionately via higher compliance costs.

Third, reputation risk, which may seem surprising given that, historically, community banks have been viewed as highly reputable by consumers. Moreover, the remarkable impact community banks had on helping our country weather the pandemic is undeniable. But to maintain our strong reputation and to continue to be viewed as trusted advisers to those whom we serve, community bankers must be forward-thinking, innovative and responsive to the evolving needs and increasingly sophisticated demands of our customers. If we are seen as failing to innovate, as subject to disruptive technologies or as falling victim to a debilitating cyberattack, much of the goodwill we have established over the years could rapidly dissipate.

Competition

Competition within the financial services industry is increasing at an unprecedented pace with no end in sight. In addition to the “traditional” competition we have always faced from commercial banks of all sizes, in recent years we have experienced increased competition from credit unions, as well as from nonbank financial institutions and digital-first providers. Pricing is as fierce as I have ever seen it, and we are noticing some competitors offering weaker loan underwriting standards and “loss leader” deposit promotions. Likewise, some of the bells and whistles related to financial technologies offered by new competitive entrants are challenging the value proposition that we offer. But that’s a good thing—for both us and our customers.

The continued consolidation of our industry is disheartening. Increasing technology and regulatory obstacles, together with other challenges such as talent recruitment and retention, will make it harder for smaller community banks to maintain an acceptable level of profitability while striving to adequately meet the banking needs of their communities. It is incumbent upon bankers, regulators and third-party financial service providers to find a way to reverse this trend and ensure the long-term viability of the community banking industry. Still, I take comfort in knowing that community banks continue to play a vital role in ensuring the prosperity of the local economies. I believe that will be the case for the foreseeable future.

Technology

The technological advances within our industry over the past decade are nothing short of mind-boggling. And I fully expect that I will be able to make that same statement 10 years hence as the velocity of change continues to accelerate. With the disruption that is sure to accompany future innovation—for example, decentralized finance, blockchain technologies, payment systems and open banking—speed and agility in changing courses quickly will be of paramount importance.

Historically, community banks have struggled to keep up with the pace of technological innovation. This is due, at least partially, to the fact that community banks are usually not positioned to develop proprietary technology solutions on their own. They are forced to rely upon core service providers and other third-party providers to deploy research and development efforts. To that end, we need not be bashful about being a “squeaky wheel” for these vendors. We must guard against relying solely on legacy information technology systems that might not provide sufficient resources to respond to the evolving needs of our customers.

There is ongoing debate as to whether fintechs should be considered competitors, potential partners or even acquisition targets. I lean toward the middle option, recognizing that we have something they want, in our deep and long-standing customer relationships, and that they have something we want, in their innovative solutions for those customers. I expect more and more of these partnerships to develop in the years ahead, and I am hopeful that they will provide a winning formula for banks, fintechs and customers.

Relationship Lending

Relationship banking will continue to be a key differentiator among community banks and our chief rivals. We are better able to serve less-conventional borrowers, often making credit decisions, at least in part, through firsthand observations of the borrower. Similarly, with less systemic bureaucracy, we often have a more efficient decision process, can offer more-flexible terms and can more quickly respond to changes in local economic conditions. Customers find solace in knowing that their primary banking relationship is with a bank that is knowledgeable about their specific needs and genuinely cares about their financial success.

But what constitutes “relationship banking” is a moving target. The rise of the self-directed consumer, and changing behaviors and expectations among borrowers are changing how lending relationships are forged. Going forward, community banks will need to be as much about "high tech" as "high touch." They are striving to create more of a balance between traditional analog customer experiences and digital interactions with a more technologically savvy customer base.

Underserved Communities

Community banks do a good job of supporting underserved communities. This is due primarily to the fact that they are, by definition, more involved in meeting the needs of their local communities than larger commercial banks or nonbank financial institutions. Can we do a better job in this area? Of course, we can. Doing so will require enhanced financial literacy initiatives, affordable pricing schedules and a coordinated effort to remove barriers to utilization. With a well-established commitment to civic engagement, and an increased awareness of diversity, equity and inclusion initiatives, I anticipate that community banks will continue to make supporting the underserved a priority. This also is a great way to increase market share and customer loyalty for the community banking industry.

With respect to revisions on rules implementing the Community Reinvestment Act (CRA), modernization efforts are welcome—provided that the final rules are applied fairly and consistently during the examination process and that appropriate flexibility and common sense are utilized in implementation. It certainly is a positive that the federal agencies are working in concert with one another to effect the proposed changes. I am particularly pleased that there seems to be an effort to tailor performance standards and data collection activities to account for differences in bank sizes, geographic footprints and business models. Nonbank financial services providers should be subject to the same levels of accountability as banks when it comes to the CRA.

Pandemic Impacts

The most significant impact of the pandemic on banks is digital transformation. This created daunting challenges for both banks and customers, but also led to rewarding outcomes. We are better bankers as a result.

The pandemic forced us to challenge our old ways of thinking and redirected our attention to our most pressing priorities, while highlighting areas of marginal importance. We now offer more and better digital and remote interactions, we have better utilization of virtual tools, and we have become more flexible in terms of hybrid and/or remote work opportunities.

With respect to regulatory examination processes, we discovered, perhaps to our surprise, that a hybrid approach has worked well and might even be preferable to fully on-site examinations. While we still enjoy and appreciate face-to-face interaction with our examiners, and believe them to be mutually beneficial, it seems that the hybrid approach has thus far proven to be effective and efficient for both parties.

Finally, with respect to ongoing legislative and regulatory support as the country emerges from the pandemic, I think the most important thing to consider is how vital community banks were to serving small businesses during the crisis, and to make sure that the constraints under which we operate are tailored to not adversely or disproportionately impact smaller banks, so as to unduly inhibit our ability to meet the banking needs of the communities we serve.

Saleem Iqbal

Saleem Iqbal is president and CEO of New York-based Habib American Bank (HAB), a position he has held since 2000. He currently serves on advisory boards of the Conference of State Bank Supervisors and the American Bankers Association, and previously served on the Community Depository Institutions Advisory Council of the Federal Reserve Bank of New York. HAB has $2.1 billion in assets. Its core businesses are commercial real estate lending and correspondent banking.

Current Risks

In my opinion, the No. 1 risk today is interest rate risk. Most community banks have been lending at 3.25% to 3.5% for the last two or three years, up until the first quarter of this year. Deposit interest rates during this period remained below 0.5%. We advertised deposit rates at 60 basis points earlier this year and had an overwhelming response. But after a month or two, the phones just stopped ringing when the Federal Reserve Board said the fed funds rate was expected to go to 3.5% by the end of this year. Consumer expectations changed. Nobody wanted to commit for longer periods. Fast forward to today, many New York banks are offering north of 2% for 12-month or longer maturities. So, interest rates have jumped so much and so quickly.

Interest rate risk management is part and parcel of banking. Before the pandemic started, deposit rates were 2.5% to 3%, up until 2019 early. Then banks got a lot of liquidity due to the stimulus. We are concerned that if deposit rates crossed 4% or 5%, many of our loans would be underwater. We have memories of the savings and loan crisis when loan rates remained fixed and deposit rates skyrocketed. That resulted in the closure of several thousand savings and loans. So we are worried about that. Hence, in my opinion, the greatest risk today is interest rate risk.

The second risk I think most community bankers or other bankers would say is cybersecurity. We have 11 IT vendors. We are a $2.1 billion bank, so I imagine that smaller banks are finding it even harder and more challenging to get all of the talent and be able to afford it all. This is definitely an important and a very high risk.

The third risk is the job market. I think every company is in the same situation, irrespective of its line of business. These are market risks; we have to deal with them.

If I have to name a fourth risk, it would be regulation, which can be a long-term challenge for a bank. Regulations just keep getting added.

Competition

When community banks compete with regional banks or money-center banks, or other community banks, that's business as usual. Depending on the products that the banks provide, stiff competition is now coming from fintechs, alternative lenders and credit unions.

This is where the playing field isn't leveled. These three have nominal to no regulation, and they're doing exactly the same things we are doing. That becomes a challenge. We don't expect much to change in the next year. However, over a three-year period, things can change, especially due to fintech and alternative lenders that are unregulated. They've been taking slices of business away from community banks, such as home mortgages. The New York Bankers Association recently said 36 million homeowners have already borrowed or taken home loans from alternative lenders. According to another study, 64% of residential mortgages are currently with alternate lenders that are not banks. So clearly this is a risk.

As far as we are concerned, we are primarily a commercial real estate lender. We're not a typical community bank. We have to focus on remaining efficient. We have to be competitive on interest rates. Our processes have to be efficient. We have to have proper market and product knowledge. If we remain that way, then the borrowers will come. This is how we are trying to remain competitive.

Technology

The community banking industry, when it comes to products and delivery channels, is very archaic. For many years, bank products have been limited to residential mortgages, commercial real estate, small-business lending, and perhaps broadly one or two more. There have not been any significant changes in the delivery channel or technology. We've been able to manage and grow nicely despite the technology handicaps.

Community banks have traditionally depended upon three core providers. Now, the core providers have improved their game in the last couple of years. I think the American Bankers Association played a very good role in making that happen. So that helps.

We are a commercial real estate lender. We do not have a heavy strategic reliance on any third party.

We use third parties for some things, but in terms of technology, we rely on the core provider. The last couple of years, however, core providers have improved their game. We've been able to manage and grow nicely despite the technology handicaps.

Relationship Lending

Let's first talk about a typical community bank. A typical community bank, as you know, will be in consumer banking products, residential mortgages, auto loans, and debit cards and everything that a consumer needs. So basically be everything for everybody to whatever extent they can.

Now, the future customers of these banks are millennials and Gen Zers. But it is yet to be seen how much value future customers will give to relationships. Or will they rather prefer anything that has better technology, ease, convenience, AI? What if they prefer to get everything done through their phones, will they really care about having relationships with the bank? Or will they just take out a loan from Google or Amazon or whoever? That is the big question, and only time will tell.

We are not a typical community bank. We are primarily a commercial real estate lender. We have two core revenue sources: commercial real estate lending on the lending side and correspondent banking services. Correspondent banking is largely relationship-driven. Commercial real estate is both.

If we look back, the U.S. has always had thousands and thousands of banks. After the Great Depression, many banks could not survive. Then, the number of banks started to increase again. Then we had the savings and loan crisis in the 1980s, and a lot of banks and thrifts failed again. Thereafter, de novos started to mushroom. But after 2008, this world changed. The number of banks has only gone in one direction. On average, we have one less bank per day.

As you can see, for the community banking model, the writing is on the wall. Whether we call it M&A or whatever, they're just dying. So, for smaller communities, they are mission-critical. Congress and regulators should consider all these things and try to support and help them.

As far as our model is concerned, it's commercial real estate. We are in New York, so it's a little bit different. Relationships matter. Many people want to do business with community banks and not with large banks because here you can talk to the ultimate decision-maker. That is why we have an edge, and that is why we still get business and we're still growing.

Pandemic Impacts

I think community banks, and many other businesses, surprised themselves by being able to work from home. Nobody was in the office, and yet the banks were running fine. That was a big lesson learned. It was a nice discovery, very encouraging.

Due to the lockdowns, which were basically government-regulated lockdowns, many community banks were concerned about their loan portfolios and that the borrowers won't be able to repay their installments. I was regularly in touch with the Federal Deposit Insurance Corp. (FDIC) and the Department of Financial Services (DFS), and they played a very supportive role in guiding us through decisions that were being made on the fly. Nobody had experience of dealing with anything like this.

From offering Paycheck Protection Program loans, to letting the banks allow installment deferral for three to six months without calling these loans "troubled debts"—each was a tremendous help to us and really commendable. We are appreciative of both the FDIC and the DFS that they let us do this, and our portfolios remained in good standing. Everything became all right after that.

Regulatory exams were also fully remote. We had safety and soundness exams with the FDIC, and we understand it must have been challenging for them also because on their side, everyone was sitting at home and our people were here. But it worked well. For the future, most bankers that I have spoken to think a hybrid model will be better in the long term. This was an emergency situation, so we had to make things work. But we want regulators to be at the bank, to see what we do, how we do it. It's much easier to explain because many things in banking are still subjective, so it's hard to explain remotely or through emails.

Bonus Question: Why should someone get into community banking?

Nobody wants to be a teller. We targeted some banks that were acquired, and their branches were being closed. So, we thought it would be so easy to get tellers in that market because the branches were now closed, and many of their employees were being laid off. But we couldn't find tellers!

I think we're talking about the Great Resignation here. People who make $30,000, $40,000 or $60,000 are saying, "How can I make the same amount of money doing something else where there is career growth as well?" This is how they're looking at things.

It is difficult for people to join community banking because it's not considered glamorous. In smaller towns, where there are less opportunities, people may opt for it. In bigger cities, it's more of a problem. This is the challenge that the industry is facing. However, for community banks with the right business model, where they have some kind of a niche, they will continue to do well and there is good opportunity for growth and future careers in these institutions.

It's important to tell our story. In the case of our bank, we've always been growing. I think if you look back over the past 10 to 15 years, we've never had a flat year. Our return on equity, over the past 15 years or so, it's never been below 8% or 9%, including 2007-09, when many banks had negative return on equity, or 1% to 2% was the peer group average. I remember in 2008 and 2009, we were still at 9% or higher.

So, for these types of banks that have been consistent and stable, there are opportunities for people. Community banking may not be as glamorous as some of professions or industries. That's what some millennials or younger folks may think. But otherwise, long term, it's a very stable career. It's very solid.

Joseph W. Conover

Joseph W. Conover is president of Northwest Bank in Spencer, Iowa. Northwest Bank, which has $2.3 billion in assets, is part of Northwest Financial Corp., which also operates another bank as well as insurance and wealth management subsidiaries. He has worked at the bank for 19 years in various roles, including branch management and commercial lending. He serves on the boards of directors of many nonprofit organizations at the local and state levels.

Current Risks

The first issue is credit risk. Right now, our metrics look fantastic as an industry. But the pending economic slowdown will test our loan portfolios. With whatever is coming at us, we are going to see whether or not we really are as good as we think we are in loan management. We also need to understand our role in our communities, making sure that we're lending where appropriate, but also not endangering the safety and soundness of our institutions.

The second issue is interest rate risk. Our asset liability committee meetings are fun again. We are having significant conversations about our position relative to increasing costs of funds, what we need to do to maintain competitiveness, what our loan yield is and where our targets are. Volatility provides opportunity for us to increase our net interest margin, but it also is an opportunity where we may be on the wrong side. We need to be nimble and flexible in managing interest rates.

The third issue, which is less apparent, but I think more problematic in the long run, is talent risk. The ability to attract smart and talented individuals into community bank settings is difficult. It's a tight labor market. We have much to offer as community banks to talented young people or people of any age. But the competition is fierce. We are a people business. Community banks sell on relationships. We must have great bankers, and without that, our value proposition erodes. To be competitive, we must double down on our people and make sure that they are trained, motivated and empowered to service our customers.

Competition

All the deposits that rained down on us from various sources, all filtering into the financial institution, created a liquidity scenario where it was all about getting loans. So, for the past year, we've really seen a very competitive market for quality loans. In the future, depositors will have a little bit more of a competitive proposition for banks as that liquidity gets sponged up.

If you pan back out to the beginning of the pandemic, I think the financial industry responded in a way that was seen as positive throughout the economy and society, highlighting the role that bankers played in supporting the economy during the pandemic and facilitating the programs that the national government implemented. Community banks performed well. Our star really was ascendant. Now, as that gets a little bit further in the rearview mirror, the aura is starting to fade. We will need to continue to make sure we emphasize relationships, so that we can continue to attract and maintain our customers.

As far as consolidation within community banking, I see some positives and some negatives. Certainly, having more choices and competition is good for the communities that we serve. But, in some cases, a combination of two organizations creates a stronger organization with sharper products and more efficient delivery. This can provide a good return for shareholders at a lower price to customers.

One part of the competitive landscape that is concerning is the specialization we are seeing throughout the financial industry. You can point out mortgage lending as an example. Another one would be lending on car titles and consumer-secured titles. These products have gotten so specialized that they are coming off the income statement for many community banks. This has created more reliance on commercial lending, small-business lending and agricultural lending than it has in the past. I am concerned with this narrowing of business lines for community banks, whether it be from competitive pressure or, in the case of mortgage lending, the burden of regulation. It makes it prohibitive for smaller institutions to be in some lines of business full time.

Technology

In the past few years, community banks have seen an explosion of fantastic opportunities to partner with technology firms as fintechs have decided to embrace the banking space rather than to dismantle it (in most cases). A lot of smart thinking has come alongside the relationships of community banks and created an opportunity for them to really innovate in digital channels.

The technology suite that is currently available to community banks is as good as it's ever been. The issue that I see is points of integration. To be able to take a best-in-class delivery system, whether it's an originating software or a software that's providing a service, whatever it is, integration to the core operating system is problematic at times. In some cases, it works great and other times it's suboptimal. I hope in the near future that integration becomes less of a choke point, and we see better and more seamless customer experiences based on best-in-class technology platforms and core operating systems.

As far as new technology, I think we've got a great suite, it's just that bringing it to the customer as a really great user experience could be better. The other component of where technology is going can be viewed from a competitive standpoint. I feel that the fintechs that once may have been looking to disrupt lending are now more apt to come alongside banks.

I think that algorithmic underwriting has been proven to be problematic. In the future, this perhaps is something that can be achieved in a different and innovative way to originate quality loan assets. But right now, it is showing its shortfalls considerably. A good underwriter, in many cases, has proven to have better results as far as loan losses in quality portfolios.

Our value proposition in community banks is smart bankers explaining financial products that improve the life of customers. And we can now do that through digital channels, whether that's an interactive teller machine, advanced videoconferencing or origination applications that connect back with a mortgage originator, a personal banker or a commercial lender. What we're really trying to do at our institution is to emphasize relationships using digital channels. We are still emphasizing that smart banker—we are not replacing him or her—but by adding the technology that's available to us, we've been able to meet customer preferences for convenience but still emphasize the banker relationship.

Very few community banks have their own software development team. And if they do, their products are very specialized. From this perspective, we're very much appreciative of fintechs. They certainly have their limitations when it comes to integration, but, by and large, we've seen some innovative steps. It is a symbiotic relationship that is absolutely vital to our competitiveness within an industry with some very large players that can develop fantastic products and digital channels. For us to compete, we need to have those third-party relationships.

Regarding cryptocurrencies, it's really about a regulatory position. Cryptocurrency may have a place in our financial system, but without a regulatory framework, it is going to be on the sideline. If cryptocurrency is ever going to be a component of mainstream financial products, it's going to have to be in a regulatory environment similar to what we deal with now. The genesis of cryptocurrency is decentralization, so the idea of having that regulated certainly is contrary to many of the purists in that industry. Cryptocurrency is all about being anonymous in a trustless environment. If that's its only value proposition, everything other than that the financial industry can do better. It's just that it's not regulated, so it's regulatory arbitrage.

Relationship Lending

Within the next three years, relationship-style banking will be extremely important as we face economic headwinds. It is as important as ever in times of turmoil—whether it's a pandemic, an economic downturn or other national or local events—that customers can turn to that trusted adviser, someone who can share their knowledge and be able to customize a financial product to an individual.

In the longer term, customers prefer to choose in-person when they want and, at other times, a "near" person, meaning maybe some video feed and then self-service. Community banks are going to be challenged with a very expensive cost structure with self-service, mobile, online banking, assisted service, automatic teller machine networks, interactive teller machine networks, maybe a call center and then full service, which is a branch network and banking originators. This is expensive, but it's our value proposition. It really is. We need to emphasize the "banker" in each one of those delivery channels, so that we can maintain relationships and add value by tailoring financial products, not necessarily a customized product, but a specific product from the suite that we have in order to meet the financial goals of that customer.

In order to be competitive, we still have to have the very best talent up and down our customer contact points. We need to have fantastic bankers that can communicate well. Our institution is working very hard on training and empowering our bankers to be able to maintain that relationship and add value.

Underserved Communities

Community banks are uniquely positioned to help serve underserved communities. Our income statements and balance sheets are dependent on their health and vitality, and it behooves us to make sure that we include them. I think that community banks currently are doing more to actively engage with all members of our community—including the underserved.

What most likely will change is the intentionality and the proactive nature of financial institutions, reaching out to the underserved rather than saying, "Here's our suite of products, and we're open for business." I think we will be asked by regulators to be even more proactive. And that wouldn't be a bad thing. But I also would like outreach to be initiated by the banking industry rather than regulated to us. The push toward the Bank On product of the American Bankers Association, and similar low-fee deposit products, is an indication that the industry can reach out to underserved members of our community.

Another part of outreach that we're doing here locally (and I serve western Iowa and eastern Nebraska), as simple as it might sound, is just making sure that we can communicate in the language that customers prefer. So, we're working very hard to increase the number of bankers who can speak in several different languages in order to make sure that we can reach those communities that prefer to bank in a language other than English.

Relative to the Community Reinvestment Act, I think that it is imperative that the regulatory environment take into account the fact that we have significantly less traffic in our branches since it is very much built around the branch network. I would invite regulators to be modernized as well, whether it's investment or lending or service. I'm very interested in knowing more about where they're going with this, and I would like to see them recognize the change in the branch structure as they go about making these changes.

Pandemic Impacts

The beginning of the pandemic was an excellent opportunity for community banks, and banks in general, to show their value. And I would like to have that framework continue, that feeling continue, in the upcoming economic downturn that we will face.

The pandemic certainly taught our institution very valuable lessons regarding the way our customers interact with the bank. Although there was still a demand for relationships, we had to adjust to different delivery channels, whether digital, telephonic or, in some cases, Zoom. We had to be creative. It really created an opportunity to fast forward a lot of these delivery channels. Some innovation was fantastic and will stay with us.

From a customer standpoint, the pandemic accelerated the move toward use of banking channels that are not in person. We're having to adjust our branches, and the layout of our branches, to make sure that they are appropriately sized for the traffic that we have now; then continue to stay connected to those bank customers through digital marketing and interaction through our digital channels.

The off-site exams during the pandemic were interesting. It certainly was beneficial to have those electronic files, that we've been working so hard to put together, accelerated. That expediated the exam process. But off-site exams are a poor substitute for being in person. I certainly enjoy the relationship with our examiners and always look to find value from them based on what we can learn from their knowledge and their insight of the industry. Our most recent exam was a hybrid exam, and I thought that was a nice mix. But the preference for in-person exams is certainly necessary.

We need to continue to examine the regulatory framework to make sure that it is allowing us to serve our customers in a fair and competitive way, recognizing that increased regulation can lead to less competition, which will then ultimately provide less opportunities for our consumers.

I believe the regulatory narrative in certain industries, for certain regulators, has become much more combative with the industry, and that is problematic. I would like to see financial institutions as part of the solution. The rhetoric around change can be done in a way that uses less vilification in vocabulary and is more of a collaborative position. I'm specifically talking about the Consumer Financial Protection Bureau request for information regarding fees. Its tone was very problematic in its adversarial rhetoric. If there is needed change, which is debatable, the tone of that conversation certainly doesn't add to an environment of collaboration.

Kim DeVore

Kim DeVore is president and CEO of Jonah Bank, a $535 million institution in Casper, Wyoming. DeVore was a founding director of the bank when it was chartered in 2006. In her long banking career, she has held positions in operations, new accounts, cash management, securities, commercial lending and compliance. She is active in community organizations including the Wyoming Business Council, Two Fly Foundation, The Lyric and the Boys & Girls Clubs of Central Wyoming. She also serves on various national regulatory advisory boards.

Current Risks

The normal three risks would be cyber (it's every banker's first because it doesn't matter what size of bank you are), the recession (credit deterioration is always a concern for community banks) and consolidation and competition. Every banker is likely going to give you those same three answers.

I try to be unique.

I feel like one of the biggest risks to the community banking model is politics entering into the regulatory environment. Regulations come, and regulations go, but this has got to be one of the times, at least in my 33 years of banking, that I see more politics entering the everyday activities of regulators.

For example, we're entering this realm of environmental social responsibility and climate risk at banks. But community banks have always been doing this. With climate risk, there's physical risk. Look at agricultural lending. Agricultural lenders are specialized. They are the epitome of measuring physical risk related to weather patterns and weather-related catastrophes. There's also transition risk. Anyone in energy lending, which our bank is, will tell you that we manage transition risk through structure. We are not oblivious to the transition that the world is going through in terms of energy. Our intent is to be good lenders; to be safe and sound lenders. We take these risks into consideration every day, but we apply them in processes that work for our bank, for Jonah Bank in Wyoming. When you start to try to put this into a regulatory framework, that's a massive risk for banks. You're going to force us into a box or force us out of a box if that happens to be our niche.

Another risk is the Section 1071 small-business-lending data collection. Community banks do 70% of the small-business lending in the United States. If you take small-business data and you expect to aggregate it down to the same level that you can aggregate Home Mortgage Disclosure Act (HMDA) data for one- to four-family residential lending, it's going to have a huge impact on our industry. For many small banks, this data collection will be similar to when HMDA got incredibly confusing and complicated. As a result, we saw many small banks exit mortgage lending. I would hate to see that happen in small-business lending.

The final risk is the potential for a central bank digital currency (CBDC) to create an upheaval in the entire banking system. What would a central bank digital currency do to our current banking system? If significant liquidity moves out of the banking system, who's going to lend? Do you want to pay private rates for private lending to the average everyday consumer? A CBDC is a risk to the community banking model, but it's also a large risk to the everyday consumer. I fear the unintended consequences of issuing a CBDC in the U.S. CBDCs are in a different risk category because it's one that we can't control. Those who support a CBDC should remember that there's a lot of consumer protection built into the United States banking system. It would take years of preparation to transition to something that offers those same protections.

Competition

We have two different sectors of competition.

First, we have our true market competition that we deal with every day. We've seen a ton of consolidation at that level. In a rural state like Wyoming, consolidation has a very large impact on our communities. You even have banks exiting some types of lending.

When regional or large banks enter our markets, our risk is that they push our pricing down. When they can't compete on relationships, and they can't compete on community involvement, they will naturally compete on price. That's where their strength lies. So, it pushes our pricing down.

On the upside, we have a lot of liquidity. And we have options in our pricing. Liquidity is cash in our wallet as a bank. So how are we going to invest it? Are we going to invest it in loans at local rates, or are we going to go buy investments? We're always going to make investments in our community, so we're always going to choose making loans. If we have to offer them at a little bit lower rate, we can handle that, especially with the rate environment pushing up margins. When rates were down at zero, it was harder to compete on price. We weren't able to get returns elsewhere to help supplement income, but now we can.

So, am I comfortable? Do I like it now? Can I live with it? Absolutely. Large banks are strong competitors on price, but community banks need to sell what they sell best, which is people and relationships and community involvement.

It's important for community bankers to recognize what they do best and not try to be everything to everyone. When we pick our niche, when we're disciplined and focused, and when we drive our products, technology and marketing around that niche, we can be very successful. There's just too much competition out there to try to be everything to everyone.

Second is what I call this whole new world of competition. We can't touch it, or feel it, and we don't see these competitors at events when we're out in the community. It's a whole new realm of competition: fintechs and crypto banks.

They pose risk to the entire banking system, but they also pose risk to community banks. We need to be aware of how these new competitors could affect what we do.

Currently, there's nothing that larger crypto organizations, or banks that bank crypto exchanges, do that impedes what Jonah

Bank does every day. They're not trying to lend in our community. But someday they might. We need to learn and understand more about these organizations, because they're not going away. The biggest mistake we could make is to ignore them.

Technology

To be honest, if I knew what technology was on the horizon, I would not be a banker.

If you were to rewind 10 or even 15 years ago, technology was more of an "or" for our customers, not an "and." A lot of banks made the mistake of having technology serve as their primary delivery channel.

As a community bank, we need to remember our niche and our strengths. Our strength is relationship banking. We should not be afraid of technology that can complement this strength. Technology can expand our horizon on who we can bank. Today, I can bank customers all over Wyoming and still see them face to face without getting in my car and driving three hours. Technology creates limitless opportunity for us.

As long as we can package technology with the relationships that a community bank can offer, we should consider adopting that technology. We need to make technology an "and" option for our customers.

Even though the impact of the pandemic in Wyoming was small, our customers started making more mobile transactions and calling in for certain things instead of coming into the bank. It appears that our customers have stuck with these changes, and we must recognize that. We need to make sure we let our customers know they have a choice at Jonah Bank. We will always answer the phone when you call, we will always say, "Hi, Joe!" when you walk through the front door. But if you don't have time to come into the bank, we have the technology that lets you continue to bank with a small bank like Jonah. Community banks can't afford to deploy all the technology that's out there, so we need to be disciplined in what we do adopt and make sure that it feeds and supports our niche.

A big aspect of the success of community banks in deploying technology and partnering with fintechs is our core service providers. Community banks need to work together to push their cores to move at light speed to create a better operating environment, so that we can plug and play and take advantage of fintech. That's where we're at a disadvantage.

Another disadvantage is that we don't have the staff and the expertise. We have 88 employees at Jonah Bank, with a good swath of expertise, and yet it took us four months recently to renegotiate our contract with our core. Four months is a lot of time, and I was very much involved. Can you imagine the loans I could have brought in, in those four months, if I wasn't engaged in that negotiation?

The core service providers have had the luxury of living a little bit behind the times on their systems, and, to some extent, we've allowed that. We need to push our cores because, right now, there is just too much risk in partnering with a startup core service provider, even if it seems to have a great product. Our entire reputation is at risk if something goes wrong with our core, because it could affect people's money. Changing your core service provider is very different from launching a cool website or deploying some new technology in some other sector. It's much harder to recover from if you make a mistake.

Relationship Lending

For Jonah Bank, if I had to quantify the value of our bank's relationships, I'd tell you it's 100%. Every bit of our business model is built on relationships. Ninety percent of what we do is small-business lending, and the best way to do small-business lending is with a relationship model.

I tell my bankers all the time: We all sell money. You might dress it up, put a different color on it, have a different slogan, but the bottom line is all banks sell money. It's how we sell it that makes a difference. Our model is completely built on relationships, and that's what we have to offer.

I can tell Joe down the street with his oil change company:

> *"You know what the benefit of banking with Kim DeVore is, Joe? I can run right down there if your credit card machine is not working or if you can't make it to the bank today and you don't have mobile capture. I'll run down and pick up your deposit. Or I'll see you when I'm in there getting my oil changed."*

When customers go through tough times, that is the prime time for community banks to advertise the relationship benefit. Think about the last two years and the economic and employment challenges that our businesses in our communities experienced. Think of the integral role community banks played in helping these businesses. In the beginning, it was the Paycheck Protection Program (PPP). Could you imagine what PPP would have looked like nationally in that first round if there were no community banks? My bankers went out and walked downtown and talked to every business to see if it had heard about the program. Our bankers stayed up past midnight to input applications, because that's when we knew the system wouldn't crash.

When your business model is relationship-based, it means that when a banker looks at a loan document and sees the name of the business, he or she knows the family behind it. Perhaps their kids play soccer together. All these different aspects play into what it means to be a relationship lender. In the end, even when the whole world went remote, relationships drove the train and they were king.

Community banks need to tell their story about how this all works. Sometimes it's nice to tell a customer:

> *"Hey, guess what? We don't have a special assets division. If you get in a tough time, your same lender is going to sit there and work with you, and she's going to meet with you every single month. She's going to help you restructure your loan. And we're going to help you through this because we're your partner."*

Community banks are not corporations. We're small businesses. We are the same people that you see every single day in your community. Community bankers are also the decision-makers in their organizations. We take care of our communities and the customers in our communities. This focus on community is also important to our employees because, honestly, it's incredibly fun to have a relationship model where you take care of your customers. I can't imagine more fun than that.

Underserved Communities

Community banks have always supported underserved markets, underserved populations, underserved industries and underserved charities. That's what we do. Quantifying this, however, is a challenge. That's why the Community Reinvestment Act has been so challenging. Community banks serve their communities daily, but not always with financial products. Financial products are the simple solution, but they aren't the overarching solution.

For example, we have some incredibly low-fee products. But the best products we have that create a better environment in underserved communities are the relationships we've built in these communities. For some underserved communities, it's related to choice and trust. I believe, community banks are best-equipped to overcome the trust barrier because we use a relationship model. We are in the community all the time. We are heading up fundraising campaigns. We are pushing to get low- to moderate-income housing built. We are the faces that you see in your community, on your school boards and on the boards of so many organizations that provide support to the underserved. We're well-positioned to provide these communities with banking services.

But how do you quantify that? The fact that Jonah Bank employees are out building homes with Habitat for Humanity, hosting a financial literacy fair or visiting all the fifth-grade classrooms in our community to teach "Being a Contributing Adult 101" is hard to quantify and put on paper. We know there's value in these things; our communities know there's value in these things as well.

Should we do more? Absolutely. Everyone should do more. I don't care if you're a banker, an investment banker, or if you are Joe who owns the oil change place, we all should do more.

That's always going to be my answer until we don't have an underserved population. I don't anticipate community banks moving away from that commitment because serving the underserved is a core aspect of what we do. It's how we build our reputations in communities, but it's also how we sleep at night.

And we need to keep pushing. We don't serve our communities because of the Community Reinvestment Act. We don't serve our communities because there are regulations that require us to. We serve our communities because we live here. When our communities thrive, our banks thrive. It's a complementary relationship between all of us.