

The Hidden Crisis in Banking
Alan J. Kaplan, Founder & CEO
Kaplan & Associates, Inc.

As we emerge from the financial downturn now known as The Great Recession, which pummeled the financial industry and spawned the now-despised program known as TARP, another crisis is looming. This crisis, however, is not one caused by faulty mortgage lending policies, credit default swaps or Wall Street. It is of our own doing, even aided and abetted at times by bank Boards and CEOs. It is a crisis of leadership, exacerbated somewhat by reticence to plan for the long term viability of our own institutions.

In the new world order of our banking industry, I believe that the two most vital ingredients for banks small and large are capital and talent. Everything else, from regulatory scrutiny to asset quality issues to investments gone sour, are tactical problems that can and will be mostly resolved over time, provided that the talent and capital are available to weather the storm. And, without these two, regulators are increasingly reticent to grant the time necessary for institutional recovery.

This is not meant to diminish asset quality and other problems which can be major headaches to fix, and may need help from a general economic recovery. We keep returning, however, to the twin necessities of talent and capital, as troubled institutions that are short on leadership will likely pay a premium for additional capital, if it is available to them at all. A number of well managed community banks have become magnets for capital—in many cases with little or no dilution—precisely because of their strong leadership teams.

According to Robert Kafafian, President & CEO of bank consulting and advisory firm The Kafafian Group, “The quality of the executive management team is one of the very first things we explore when working on a strategic plan for a client. If a bank lacks strong players in critical positions, it makes executing the plan much more challenging, especially when approaching a transition in any of the bank’s senior leadership roles. While planning is important, having a team that can execute is critical.”

Having been in countless bank boardrooms and advised dozens of community banks around the issues of leadership succession, some patterns have emerged:

- Most Bank Boards with a named successor have limited context with which to determine whether that individual is truly ready and capable of running the bank, or whether this person can create “followership” throughout the organization.

- Many incumbent CEOs are reticent to truly plan for their departure, because they are not sure when they will really want to retire; or they do not want to be “pushed” by someone waiting in the wings; or they simply refuse to accept that they will not live forever.
- Boards often struggle with the issue of “the devil they know”. We have seen many Boards select a less ready internal successor, who is a good team player and wonderful cultural icon, over a more qualified (and well fitting) outsider, simply because they were not willing to hire someone they did not know prior to launching their search. If a Board strongly desires a home grown successor, which is usually preferable, the process of developing the next leader must begin much sooner.
- Banks too often begin to search for a successor with a short timeline for the incumbent CEO to retire. An earlier hunt for the future leader would allow for better successor development, a smoother cultural integration, and an easier transition in partnership with the retiring CEO.

So, what is the solution to this conundrum? The answer is quite simple: invest the time early-on to develop the high potentials within your organization; set the expectations around timelines and roles; and be honest about what you have or do not have in your own talent pool. Banking today is a far more complex industry that it was in the mid-1980’s when I first entered the industry. The demands on CEOs of even the smallest institutions require broader skill sets, new ways of managing a diverse and diffused workforce, and political and organizational savvy on a new level. Developing these qualities is not easy, but failing to do so actually creates more institutional risk, including the complexities involved in bringing in a new leader from the outside when internal development efforts fall short.

We have noticed a decline in attendance at industry conferences over the past few years, partially due to the cost climate and partially the “optics” of a Board or bank leaders flying off to a resort on “bank business”. However, industry conferences and conventions—some of which clearly offer stronger education than others—can provide a vital connection to the latest trends and issues facing those with fiduciary responsibility for the institution. The ABA, ICBA, FMS, RMA, BAI and countless state associations (we currently belong to seven) provide excellent training programs for both up-and-comers as well as incumbent leaders. More banks should leverage these and other regional and national resources on behalf of the next generation.

Back home, few boards are focused on the two most vital elements of grooming and retaining high potential executives:

1. The personal involvement of their boss (or Board) and
2. Providing developmental stretch assignments for up-and-comers.

This is where the objections often start, with comments like “I can’t afford to take my Chief Lender out of that role to broaden her background. I need her there”. We believe that if she is a true successor contender, you can’t afford NOT to round out her banking skills and knowledge in other key areas of the institution. We have seen too many solid citizens elevated into the President’s chair with less than ideal preparation, where the bank could have invested the time (more than money) to better round out their experiences. A little coaching around leadership competencies and managing former peers doesn’t hurt either, and is often a very worthwhile investment. *Most underprepared successors will be the first to admit that they wish more had been done to prepare them for the Big Chair.*

Showing your up-and-comers that there is a plan for their future, and that you as their current leader (or as a Board Member) are consciously aware of this, is also vital. High potentials want to “feel the love”, and this more than anything will keep them committed to the organization. Few rising stars will leave an institution that they feel cares about them and is working to help them reach their potential. Developmental stretch assignments, special projects, and Board exposure are all ways to make your best-and-brightest feel valued—while while testing their mettle. Best of all, these activities do not cost the bank money to implement; they may actually save or make money for the institution.

Adds Kafafian, “Community banks can do more to prepare for leadership succession well in advance of planned retirements. Failing to groom the next generation can be one more reason why a bank might be forced to consider selling or merging.” In the future, when the current financial industry downturn is finally in the rear view mirror, there will likely still be between 7000 and 7500 banking institutions in this country. Yet it is unclear whether there will actually be enough qualified leaders to run these banks. Formal training programs like the one I was recruited into right out of college have largely gone by the wayside.

Today, what remains are mostly a handful of larger community banks with a few credit analysts being training on-the-job. While there is nothing wrong with this approach, it lacks the scale and depth of predecessor programs. Quality commercial loans may be hard to come by these days, but quality commercial lenders with strong banking skills and upside potential are even harder to find. Yet this is a major part of the talent pool from which future bank leaders will be drawn.

Our industry remains a vital part of the national economy in many ways, and community banks are often the lynchpin of their local business communities. Ensuring the survival of the industry and community banking is critical all across the country. The best way to secure your bank’s future is by developing leaders within the bank who have the potential to manage and grow a strong, healthy institution for the long term. Failing to do so may result in your bank’s next crisis, and one which may be even more difficult to resolve.



Alan J. Kaplan is Founder & CEO of Kaplan & Associates, Inc., an executive search and talent consulting firm specializing in the banking industry. You can reach him at 610-642-5644 or alan@kasearch.com.