



**THE
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...helping banks perform better™

*Jeffrey P. Marsico,
Executive Vice President*

Enhancing Operating Efficiency

June 11, 2009

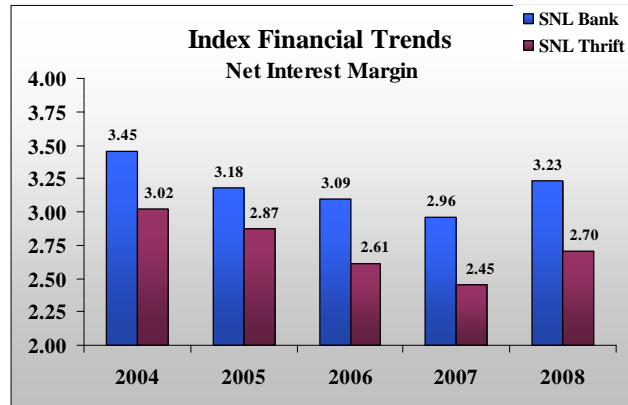


Presentation Outline

- Reasons for Efficiency
- Identifying Your Need
- How to Conduct A Profit Improvement Study

Reasons for Efficiency

Revenue growth has become more difficult for banks

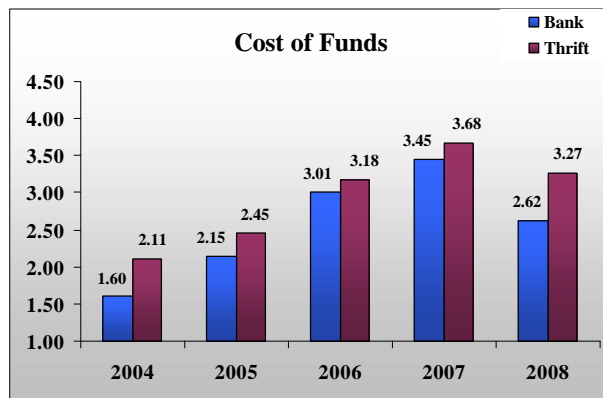


Source: SNL Financial Index Data

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Reasons for Efficiency

Revenue growth has become more difficult for banks



Source: SNL Financial. Data compiled from all publicly traded banks and thrifts listed on a major exchange.

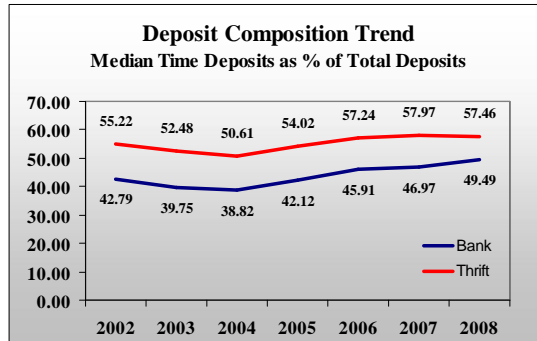
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Reasons for Efficiency

The rise in cost of funds is driven by more than rates

The structure of balance sheets is changing

- Time deposits became a larger part of deposit portfolios over the last five years.



Source: SNL Financial. Data compiled from all publicly traded banks and thrifts listed on a major exchange.

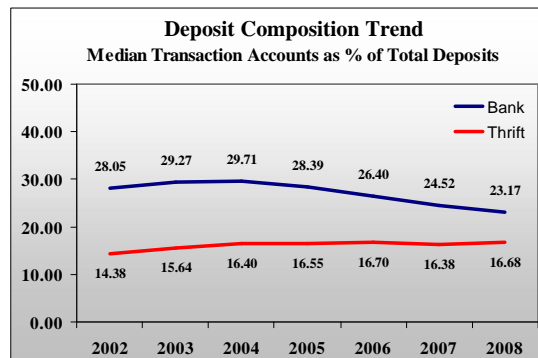
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Reasons for Efficiency

The rise in cost of funds is driven by more than rates

The structure of balance sheets is changing

- Transaction accounts' portion of deposits is flat or declining



Source: SNL Financial. Data compiled from all publicly traded banks and thrifts listed on a major exchange.

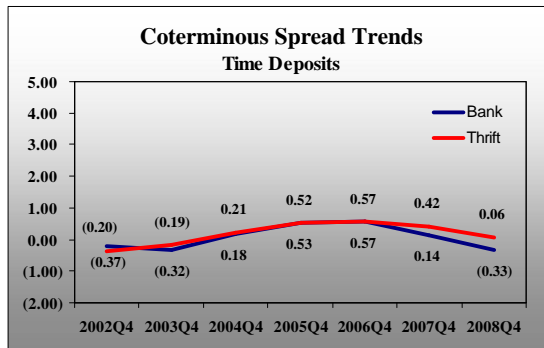
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Reasons for Efficiency

Net interest margins are harder to maintain

Deposit portfolios in particular are becoming less profitable

- Although CD's are a greater portion of bank balance sheets, they are contributing less to spread



Source: The Kafafian Group, Inc. proprietary database of profitability outsourcing client data. Coterminous spreads are determined by comparing bank rates at the customer account level with wholesale rates of similar terms. The typical source of the rates is the Federal Home Loan Bank.

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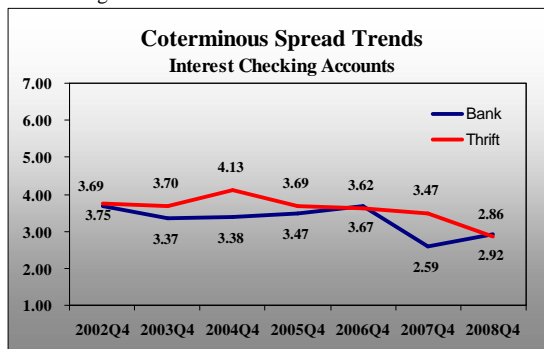
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Reasons for Efficiency

Net interest margins are harder to maintain

Deposit portfolios in particular are becoming less profitable

- Core deposit spreads have not compensated for the decline in overall deposit spreads driven by relative CD growth.



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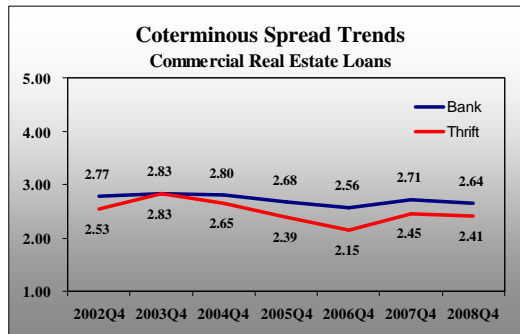
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Reasons for Efficiency

Loan spreads are not increasing to compensate

- Both commercial real estate and residential 1-4 mortgage spreads have been declining over the last five years.
- Increased credit quality costs will impact income statements.



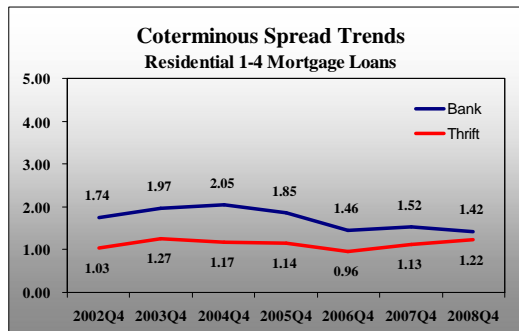
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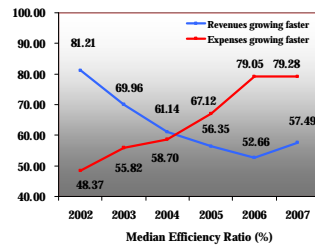
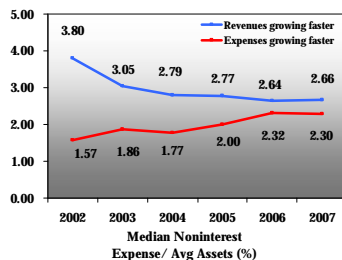
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Reasons for Efficiency

Maintaining the growth of expenses in relation to revenue has a dramatic effect on financial performance

- Institutions where revenues grew faster than expenses start out with worse financial performance, BUT...
- Their bottom line performance quickly outpaced the institutions where expenses grew faster, whose performance suffered greatly.



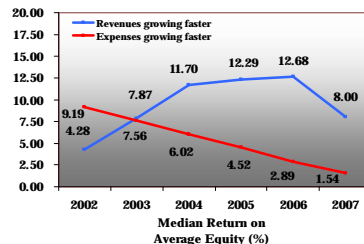
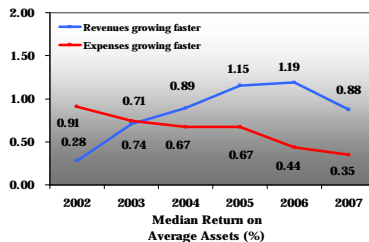
Criteria: Banks and thrifts where the difference between the compound annual growth rates (CAGR) of operating revenue and non-interest expense for the years 2002 to 2007 either INCREASED 10% or DECREASED 10%. The rates for 2008 were excluded from the selection criteria due to anomalous results.

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Identifying Your Need

- Peer Analysis
- Comparatives
- Trends
- Benchmarking

Identifying Your Need

Peer Analysis

For the LTM ended March 31, 2009

Company Name	Net	Yield on	Non-Int.		Efficiency Ratio (%)	ROAA (%)	ROAE (%)	
	Interest Margin (%)	Earning Assets (%)	Cost of Funds (%)	Expense/ Avg. Assets (%)				
1 Bank Mutual Corporation	2.28	5.26	3.21	1.82	65.78	0.55	4.75	
2 Citizens First Bancorp, Inc.	2.85	6.22	3.46	2.94	78.12	(2.90)	(36.22)	
3 First Defiance Financial Corp.	3.79	6.06	2.30	3.04	64.23	0.38	3.57	
4 First Place Financial Corp.	2.96	5.79	2.88	5.44	69.95	(2.86)	(32.54)	
5 HF Financial Corp.	3.41	5.97	2.64	3.03	72.84	0.68	10.12	
6 HMN Financial, Inc.	3.10	5.88	3.05	2.79	64.84	(1.27)	(14.44)	
7 NASB Financial, Inc.	2.80	6.11	3.58	2.70	58.88	0.84	8.48	
8 United Community Financial Corp.	2.93	5.73	3.01	4.35	72.19	(1.34)	(13.61)	
9	25th Percentile	2.84	5.78	2.82	2.77	64.69	(1.72)	(18.97)
10	75th Percentile	3.18	6.07	3.27	3.37	72.35	0.58	5.68
11	Average	3.02	5.88	3.02	3.26	68.35	(0.74)	(8.74)
12	Median	2.95	5.93	3.03	2.99	67.87	(0.45)	(5.02)
13	Your Bank	3.81	6.41	3.05	3.41	79.56	0.58	2.87

- Highlighted bank has a net interest margin higher than peers.
- Overall performance suffers due to higher expense and efficiency ratios.

Identifying Your Need

Comparatives

RETAIL BRANCH RANKING REPORT 4TH QUARTER 2008

Branch Office	Deposits	Deposit Size Rank	Earning Assets	Earning Assets Rank	% of Deposits Rank				
					Net Liability Spread	Non-Interest Income	Direct Expense	Total Non-Int Expense	Net Income
Washington	188,142	1	343,314	1	10	4	7	7	1
Jefferson	94,450	2	162,892	2	11	9	8	8	8
Grant	55,980	3	104,241	3	7	1	9	9	12
Monroe	54,639	4	55,813	5	12	10	1	1	4
Lincoln	41,666	5	20,391	7	4	8	3	2	6
Jackson	38,189	6	64,488	4	5	3	11	11	9
Tyler	31,071	7	11,573	9	1	6	6	6	7
Madison	27,230	8	36,194	6	2	7	2	5	3
Harrison	18,331	9	8,642	10	3	2	4	4	5
Van Buren	17,572	10	3,303	11	8	11	12	12	11
Polk	13,359	11	1,625	12	6	12	5	3	10
Adams	13,084	12	12,460	8	9	5	10	10	2

Average Branch Size **49,476**

Source: The Kafafian Group, Inc. proprietary database of profitability outsourcing data.

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Identifying Your Need

Trends

Non-Int. Bearing Business Demand Product	1Q	2Q	3Q	4Q	5Q
Credit for Funds	4.86 %	4.09 %	3.83 %	3.95 %	3.50 %
Interest Expense	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %
Total Interest Spread	4.86 %	4.09 %	3.83 %	3.95 %	3.50 %
Funds Credit Allocated Equity	0.15 %	0.15 %	0.15 %	0.18 %	0.15 %
Net Interest Spread	5.01 %	4.24 %	3.98 %	4.13 %	3.65 %
Non-Interest Income	0.89 %	0.88 %	1.04 %	1.25 %	1.04 %
Total Income	5.90 %	5.12 %	5.02 %	5.38 %	4.69 %
Non-Interest Expense	2.08 %	2.26 %	2.22 %	2.72 %	2.11 %
Pretax Profit (Loss)	3.82 %	2.86 %	2.80 %	2.66 %	2.58 %
Pretax ROE	127.27 %	95.22 %	93.15 %	89.05 %	85.74 %
Number of Accounts	4,584	4,622	4,633	4,645	4,685
Average Balance per Account	\$18,900	\$18,204	\$18,579	\$15,280	\$20,136
Non-Interest Income per Account	\$42.49	\$39.74	\$48.07	\$48.14	\$52.51
Annualized Cost per Account	\$393.86	\$411.21	\$412.66	\$414.87	\$424.63
Annualized Net Income per Account	\$721.60	\$519.92	\$519.13	\$408.25	\$517.98

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Identifying Your Need

Benchmarking

BENCHMARK COMPARISONS

	Your Bank	Survey Participants		
		Median	Low	High
Teller transactions per teller FTE/mo.	1,675	2,175	1,614	2,682
New accounts opened per platform FTE/mo.	30	48	32	68
Average total cash per branch	\$375,126	\$319,513	\$279,342	\$450,086
Assets supported per finance/accounting FTE	\$333,000,000	\$173,000,000	\$123,000,000	\$234,000,000
Mortgage loans serviced per servicing FTE	497	984	740	1,474
Bank headcount per human resources FTE	92	89	75	104

Source: Cornerstone Advisors

How to Conduct a Profit Improvement Study

- Review strategic direction with respect to your Institution's anticipated growth, lines of business, product offerings, customer service expectations, competitive environment, geographic diversification, and other operating issues and opportunities.
- Form a profit improvement team with individuals from each department to interview line and staff personnel relative to Senior Management's goals and objectives.

How to Conduct a Profit Improvement Study

- Review all major departments including: retail banking, lending, fee based lines of business, marketing, IT/systems and operations support, corporate, finance/accounting, human resources, auditing.
- Review processes and procedures for best practices.
- Compare operating costs and ratios of key lines of business, departments and divisions to financial industry databases.

How to Conduct a Profit Improvement Study

- Evaluate banking relationships, other outsourcing relationships, contractual relationships, vault cash, float/cash management and service fee, and other pricing issues.
- Obtain buy-in of final recommendations, if at all possible, with department heads.
- Document resulting conclusions and recommendations highlighting efficiency opportunities, cost benefit, and prepare a detailed implementation plan.
- Review documented conclusions and recommendations with Senior Management.

Scope of Study Approach

- Set target dates for all personnel on the Profit Improvement Team to complete initial interviews, document findings and finalize recommendations.
- Meet bi-weekly to review status, findings to-date, items to obtain, implementation approval.
- Do not waste time and effort on areas where there is little or no efficiencies to be gained.
- Work with employees in the area to obtain their cooperation and agreement.

Profit Improvement Techniques

- Develop position tasks, time involved and volume for daily, weekly, monthly and on request activities.
- Ask the same question to both the supervisor and clerk to assure the answers are similar.
- Determine if duplicate data is entered into two different automated systems.

Profit Improvement Techniques

- Review any manually performed activities to determine if they can be automated.
- Evaluate if any branch activities can be centralized or should centralized functions be accomplished in the branches.
- Develop overall time and effort involved with creating/manipulating management and board reports.

Vendor Analysis

- Review all YTD total vendor payments.
- Research contracts for end dates and penalty clauses.
- Determine which departments utilize vendor's services.
- Obtain detailed invoices on specific vendors.
- Evaluate if vendor services are still required or can they be accomplished in-house.
- Determine if it is appropriate to obtain competitive bids.

Outsourcing Functions

- Trust/Wealth Management System
- IT Processing
- Item Processing
- Internal Audit
- Loan Review
- Internet Banking
- Statement Printing
- Messenger

Common Areas for Potential Savings

- Deposit Operations
- Branches
- Cash Management
- Loan Administration/Operations
- Wealth Management
- Incentive Programs
- Service Charge Fees

Typical Profit Improvement Findings

- Reduce bank cash requirements.
- Increase/Add service types and fees.
- Reduce branch staffing and overtime.
- Reduce deposit operations/loan operations personnel.
- Evaluate accounts with waived fees.
- Modify courier and ATM loading schedules.

Reduce Overall Bank Cash Requirement Tasks

- Obtain detail general ledger daily balances for branch teller, vault and ATM cash.
- Analyze branch teller draw and vault compared to present limits.
- Review limits to determine if they should be lowered.
- Analyze ATM loads and holdover cash.
- Evaluate internal versus outsourcing ATM loading and maintenance activities.
- Review armored car schedule and costs.
- Calculate potential cash savings based on the current federal funds rate.

Typical Bank Cash Requirement Findings

- Branch teller draw and vault limits too high.
- Floating/Temporary teller draws not cashed out.
- Branch limits too high and not monitored.
- Armored car invoices not reviewed.
- Different vendors providing ATM and branch cash.

Profit Improvement Alternatives

- Conducting the study
 - *Internal bank personnel*
 - *Management consultants*
 - *Combination of both*
- Implementation recommendations
 - *Non staffing issues immediate*
 - *Staffing reductions at end*
 - Through attrition
 - At one time

Profit Improvement Alternatives

- Sharing Savings
 - *Internal bonus pool*
 - *Percentage of savings*
 - *Fixed fee*
 - *Fixed fee with guaranteed minimum savings*

Profit Improvement Conclusions

- Constantly evaluate your own bank
- Utilize peer, trend and benchmarking techniques
- Manage costs, don't simply cut costs

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