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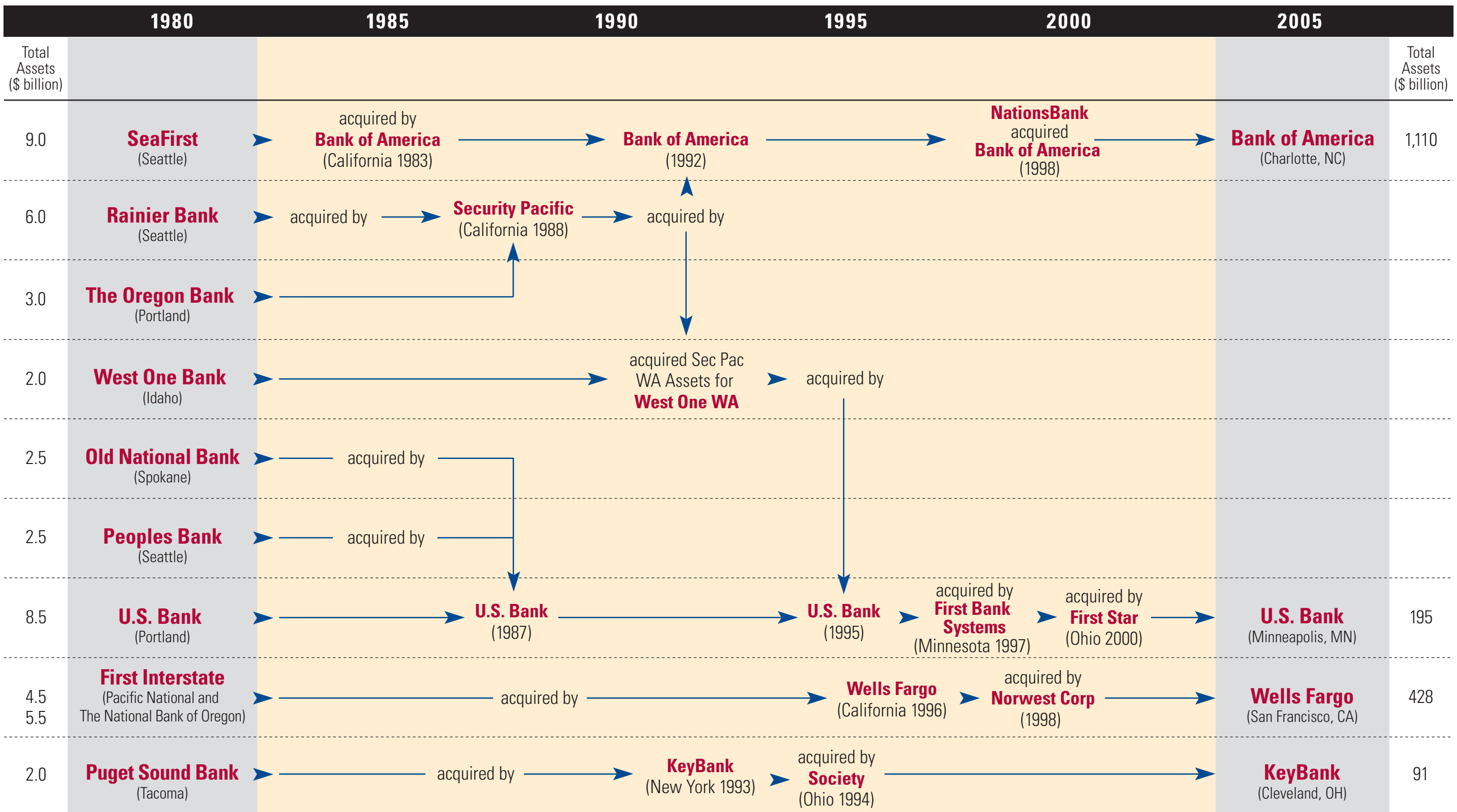
Northwest Banking Transformation

With the barriers to interstate banking falling in the 1980s, bank mergers dramatically changed the look of Northwest banking. Here's a look back.

by Michael T. Newsome



Northwest Banking Mergers and Acquisitions: *A look back over the last 25 years of the changing bank scene in the Northwest.*

Looking back over the past 25 years that we have closely followed the banking industry, a quick retrospective provides a reminder of just how radically the Northwest banking landscape has been transformed. As the result of this makeover, discriminating users of commercial banking services probably have more options than ever before.

In 1980, Northwest businesses were served by less than ten institutions, most headquartered in Seattle or Portland. Seafirst was the leading bank in Washington followed by Rainier, Peoples, Old National (Spokane), Puget Sound (Tacoma), and Pacific National. U.S. National Bank was the dominant Oregon presence and First National Bank of

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Oregon and The Oregon Bank were significant players. At the time, interstate banking was a topic of great interest to bank executives, but it was not clear when and how the regulatory barriers to multi-state banking would fall. Since the 1940s, banks were confined to operating branches and taking deposits in a single state. There were a few notable exceptions, such as Western Bancorporation, the predecessor to First Interstate Bank, a bank holding company that owned banks in eleven western states, including Pacific National Bank in Washington and the First National Bank of Oregon.

The hurdles to interstate banking began to erode in the early 1980s as many states liberalized in-state branching restrictions and began to authorize bank holding companies to make cross border purchases of banks. As a result, merger activity blossomed and a number of banking firms set out to build

(continued p.2)

regional franchises. In 1994, the Riegle-Neal Interstate Banking Act was passed, wiping away all interstate-banking restrictions and igniting a wave of consolidation and integration that continues even now.

Mergers have generally occurred across markets, rather than within them, as bank regulators have been particularly sensitive to the creation of large local concentrations and impairment of competition. A case in point is the merger of Bank of America and Security Pacific in 1992, which combined the two largest commercial lenders in Washington —Seafirst and Security Pacific WA (Rainier). In order to win approval of the deal, Bank of America divested much of Rainier's Washington commercial loan portfolio and many of its branches. The acquisition of these assets propelled Idaho-based West One Bank into a significant position in the Washington market.

TECHNOLOGY A DRIVING FORCE

In large measure, the fundamental force driving banking industry consolidation has been technology. Data processing and communications technology, through the use of very large databases, call centers and ATM networks, made it possible to centralize and dramatically reduce the cost of backroom operations and customer service units that are core to retail (consumer) banking.

For middle-market and small businesses, where credit needs are the major concern, service is predicated on local relationships with individual bankers. Here, the strategy of "bigger is better", and therefore "really big must be much better", has not proven to be as compelling. The drive for economies of scale in commercial banking has been manifested in the standardization of products, services and decision making. And, wherever possible, both customer service and decision making has been centralized so as to handle more volume with less staff. For example, every major Seattle bank used to have local trade finance capabilities to handle import and export transactions. While these services remain readily available, the vast majority of the work is no longer handled locally.

BANK HEADQUARTERS RELOCATE

The fact that no major bank makes its headquarters in Washington or Oregon (save Washington Mutual, which exited commercial banking last year) has had, perhaps, the most important impact. Policy is no longer made in the Northwest and the policy makers in Charlotte, Minneapolis, San Francisco, or Cleveland are not intimately connected to Northwest business people. Every major bank will tell you that the bulk of their credit decisions are made within the local market. This is true, but these decision makers are on a much shorter leash because the banks' credit policies are much more comprehensive than in the past. Bank-wide lending policies are prone to change without much local input or notice. This makes the rules of the game less predictable. Some will argue, but it is fair to say that local bankers at the major institutions do not have the same degree of discretion in serving the needs of their customers that they once enjoyed.

PERSONNEL TURNOVER

The other notable effect of bank mergers is personnel turnover, which has always been a challenge for large banks. The issue has intensified in the sweep of mergers. For many companies, the process of "educating" their bankers is a familiar, even routine, experience. The result is that the bonds that once existed between the local predecessors of the national bank goliaths and their customers have weakened.

REGIONAL BANKS STEP UP

One might think that all the shuffling and consolidating over the past 25 years has changed the competitive environment to the detriment of the commercial borrower. In fact, the impact has not been quite as negative as this seems to suggest. The complexion of the market has been altered – BofA is not the Seafirst of old, just as U.S. Bank today bears little resemblance to its Northwest predecessors, U.S. Bank of Oregon and Peoples Bank. Nevertheless, the Northwest banking market may be as fiercely competitive as ever. The mega-banks have developed capabilities that better serve certain customer segments, particularly large companies with operations in multiple states or overseas, in certain industry specialties, or requiring syndicated credit facilities. Asset-based lenders, once minor players in the market, now finance the challenging situations that are defined by fast growth, high leverage or deteriorating performance. Competent regional banks, such as Banner Bank, Washington Trust, First Mutual, Columbia Bank, Commerce Bank and Sterling Savings, have emerged to fill the gaps left by the mega-banks and are aggressively courting middle-market companies. And, a number of community and newly chartered startup banks are targeting small businesses. Many of the more-seasoned lenders that came up through the ranks of the mega-banks have migrated to these institutions. These banks offer genuine expertise and flexibility.

There is an abundance of alternatives, though not every bank is a fit for every situation. It's our advice that choosing a bank should be the result of a thoughtful analysis of the needs and attributes of the business. The best results are usually achieved through a competitive selection process. ❖

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ABOUT ZACHARY SCOTT

Zachary Scott is an investment banking and financial advisory firm founded in 1991 to serve the needs of privately held, middle-market companies. The firm offers a unique combination of in-depth knowledge of the capital markets and industry competitive dynamics, sophisticated analytical capabilities, and proven expertise in structuring and negotiating complex transactions. For more information on Zachary Scott, please go to ZacharyScott.com.

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