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Financial Services Industry Getting Stronger In 2011



Blake Christian, partner at Holthouse, Carlin & Van Trigt, and Regina Grant Peterson, executive director of Advantage Certified Development Corporation, work in Downtown Long Beach's financial district that includes many accounting offices, brokerage firms, insurance companies, investment managers and related financial services industry businesses. A number of banking institutions line both sides of Ocean Boulevard, including Beach Business Bank, California Bank & Trust, CapitalSource Bank, Chase Bank, Citibank, City National Bank, Comerica Bank, First Bank, Union Bank, U.S. Bank and Wells Fargo, while Farmers & Merchants Bank is headquartered downtown on Pine Avenue and International City Bank is headquartered downtown at Ocean and Long Beach boulevards. (Photograph by the Business Journal's Thomas McConville)

■ By **TIFFANY RIDER**
Staff Writer

In 2011, local executives agree that the financial services industry will strengthen with the stock market remaining bullish, along with the added benefit of the extension of Bush-era tax breaks while lending begins to loosen.

Although 2010 saw more bank failures than any other year since 1992, those banks that survived the recession are lending and getting stronger.

According to Rod Banks, executive vice president of commercial banking services for City National Bank, the institution bought two banks in San Diego and one in Nevada in the past two years. "Banks like us and other healthy banks have gone out and acquired those institutions that failed and filled in specific markets," he told the Business Journal.

Farmers & Merchants Bank, based in Long Beach, saw record profits in 2010 and is looking to expand into two more locations in 2011, according to CEO Henry Walker. "We've had fabulous growth over the last three years in assets," Walker said. "When your niche is service and safety, times like this play into our hands very well."

In preparation for an improving economy, Banks said City National is starting to replenish its sales force. As a whole, he said the banking industry is likely to selectively hire for key markets. "I think that's one of the things that we see, is while most companies have improved their bottom line by cutting expenses, I think there is still just too much unemployment out there," Banks said. "That's what's going to stick with us for a while. We just need to get people back to work."

Both Walker and Banks agree the banking industry is doing better as the Southern California economy begins to stabilize and banks begin to adhere to stricter reporting requirements per the federal financial reform act.

"We've had to reset values in a lot of areas, and that reset is going to allow businesses again to go back out and make deals," Walker said.

Banks said because more banks are flush with cash these days, they are putting that cash to work back into the community. "These loans [today] are far better for the bank and far better for the community," he said.

Businesses were investing in 2010 and will continue to invest in 2011, according to Nancy Sidhu, chief economist for The Kyser Center for Economic Research of the Los Angeles County Economic Development Corporation. Businesses have waited out the economic storm to purchase new equipment and technology, and banks are poised with a greater willingness to lend to quality borrowers today than they were in 2008 and 2009.

According to Banks, for the right client and borrower, City National Bank has been and continues to lend. "Last year was a good example for us," he said. "In 2010 our lending efforts, for the first three quarters of the year, were literally double what they were the prior year."

Small businesses looking to expand or buy real estate have the option of taking out a federal SBA 504 loan. Advantage Certified Development Corporation (CDC) offers such loans, which tend to measure jobs better than the standard SBA 7a loan, according to the company's executive director, Regina Grant Peterson. "One of the things that we have prided ourselves in is, that as of the end of this month, we've been in business for 32 years and our loans have

helped to retain and create more than 20,000 jobs," she said.

The loan structure at Advantage CDC is typically 50 percent from the bank, 40 percent from the federal program facilitated through Advantage CDC and 10 percent from the borrower. "Most borrowers have to put in about 25 percent for conventional financing," she said. "With this low down, they are able to save more of their money and use it for working capital."

Advantage CDC works with 30 to 40 different lenders. Some recent transactions they have made to help Long Beach businesses include assisting the Kress Market relocation from Compton to 433 Pine Ave. with Farmers & Merchants Bank, the Consumer Legal Services relocation from Santa Monica to 2330 Long Beach Blvd. with Bank of America, and the Law Offices of Brian Lerner relocation to 3227-3233 E. Broadway with Wells Fargo Bank. These SBA 504 loans are assumable, which makes the program all the more attractive, Peterson said.

"Even in this economy, we're still finding that there are still quite a few good deals out there," she said. "It's just a matter of the businesses feeling that the time is right for them to move. Many of them are making some really good decisions because, with real estate values being low, it is a really good time for them to think about owning their own property."

Stock Market Stable, Investments Climb Slowly

The stock market did well at the close of 2010, which has helped to boost projections of economic recovery for 2011. The attitude remains bullish for 2011 in all areas except for housing, and the nation is poised for strong gross domestic product (GDP) growth, according to Lisa Petrie, senior vice president of investments with The Petrie Financial Group, a UBS Financial Services team in Long Beach.

"If you look at the marketplace today, we're running at a price earnings ratio of 13 times earnings," she said. "That's where we expect to end in 2011, except that we do think that the corporate numbers will come in a little bit better."

Petrie expects earnings to be at 11 or 12 percent this year, with a slight drop expected in 2012. Because interest rates have already gone up in 2010, Petrie does not expect the U.S. Treasury to drastically move it up this year. Through June, the Federal Reserve plans to purchase \$600 billion in bonds in order to keep long-term interest rates low and stimulate investments and consumption.

Currently, revenue growth is in line with normal GDP, which contributes about six percent anyway, and then margins have expanded a great deal in 2010. That expansion should continue in 2011 as the economy stabilizes, Petrie said. "I actually think there will be solid money flow with net equity growth this year," she said. "That's coming from the marketplace itself as well where you've got companies doing buybacks and in raising dividends with cash that they have been accumulating over the last couple of years because of all the uncertainty. That alone will probably add money into the market itself, which is obviously going to be beneficial."

Tax Breaks Extended, Bodes Well For Growth

Every W-2 employee saw a slight increase on his or her paycheck after January 1, thanks to the extension of the Bush-era tax cuts by President Obama. The government went from 6.2 to 4.2 percent employee portion of the FICA tax, which could result in adding a thousands dollars of additional cash over the course of the year, according to Blake Christian, partner at public accounting firm Holthouse, Carlin & Van Tright. "In light of the deficit, I think that payroll tax break may not have been necessary," he said, suggesting that the break should have come with a cap to not allow

high income earners making more than \$100,000 to benefit

Overall, Christian said the extension of tax cuts gives comfort to business owners and middle and high income taxpayers, which bodes well for capital investment and job growth.

John Di Carlo, partner with Windes & McClaughry Accountancy Corp., agreed. "It also adds some stability into the economic decisions when you are making analysis of either personal finances or business finances," he said. "The challenge is going to be what happens after the next two years, if we're going to again wind up with a last-minute decision about what the 2013 rates are going to be." Di Carlo said he hopes the tax breaks allow people to spend more on consumables and that businesses consider investing in expansion.

Residential energy tax credits have been reduced from 30 percent down to 10 percent with an overall cap of \$500 down from \$1,500, which Christian said is "unfortunate when everyone is focused on greening the country." Business credits for investing in energy efficient equipment have not been reduced.

Both Christian and Di Carlo agree that the most significant change this year are the new rules on estate taxes and gifting, which provide a \$5 million lifetime exemption for both. "It's going to allow an opportunity for people who have that kind of wealth to look at what their options would be in terms of making lifetime gifts over the next couple of years," Di Carlo said, referring to transfers of property and business. Christian said the \$5 million exemption and tax rate of 35 percent are both very fair. "It was a really tough year in 2010 to do estate planning because nobody knew what the rules were," he said. "At least we have a clearer picture now of what rates are and what the exemption amounts are."

Insurance To Remain Flat With Some Uncertainty

Local insurance broker Kelly Williams III, CEO of Kelly Williams Insurance, said he thinks 2011 should show more of the same on the commercial insurance side while workers' comp, health and employment practices insurance continue to climb. Pricing remains flat as the economy crawls toward recovery, but Williams said premiums would increase when businesses begin to rehire and gross revenues increase. "I see a better outlook than last year, but pricing is pretty similar outside of workers' comp, health and employment practices," he said.

Peter Moraga, spokesperson for the Insurance Information Network of California (IINC), said commercial lines are expected to remain flat, with experts estimating only about 5.4 percent growth by 2012. The future of property casualty insurance is uncertain as changes loom.

Property casualty insurers contribute about \$30 billion to California's gross state product, according to the IINC, and the state collected \$2.05 billion in premium taxes from insurers in 2009 – nearly double that of the next leading state. On the homeowner's insurance side, agents continue to work with clients to provide information about disaster prevention and are concerned that few homeowners have earthquake coverage – about 11.9 percent, according to the IINC. Property casualty insurers also cover about 24 million cars in California, more than any other state. For auto insurance, the IINC reports a new type of pay-as-you-drive policy is being offered in California by select insurers based on miles driven, which could cut costs for those who don't drive as much. ■