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Becoming Mr. Mainstream

Hanmi Financial chief executive Sung Won Sohn, who made his name as a Wells Fargo economist, is seeking to make over the biggest institution in the Korean-American bank niche. He faces stiff competition from Wilshire Bancorp, Nara Bancorp and Center Financial, all of which also have profited from their entrepreneurial client bases and a sizzling southern California economy. Like all red-hot markets, there's always room for improvement, and, some observers argue, likely consolidation in a market driven less by geography than ethnicity. Will Sohn use his Wells experience to broaden his reach?

Sung Won Sohn grew up in small-town Korea during the 1950s, the son of a bank president. Back then, bankers' families often lived in houses attached to their institutions, and Sohn's was no exception. Times were tough, and the young Sohn would sneak into the bank on weekends with his siblings to make paper airplanes and draw pictures. "We weren't supposed to do that," Sohn says conspiratorially. "Paper was very scarce and very expensive." On workdays, employees would stash their lunch boxes, filled with rice and relishes, in the cafeteria. "We would go in and open up their lunch boxes to see who had the best relishes," Sohn recalls. "My father found out, and he really scolded us." It might be difficult to imagine Sohn, who became a renowned economist for Wells Fargo & Co., as a young troublemaker. Rest assured, he's putting that rebellious streak-and a diverse background-to good use as CEO of Los Angeles-based Hanmi Financial Corp., the nation's largest Korean-American bank.

Since taking \$3.7 billion-asset Hanmi's helm two years ago, Sohn, 62, has sought to turn the operating model for a Korean bank on its head, making it more like a mainstream U.S. bank. That means, among other things, expanding a limited product menu, introducing incentives to encourage cross-selling and abandoning the father-knows-best organizational structure that's common fare among many Asian-American banks. "The typical Korean organization is very militaristic: 'I'm at the top. Do what I tell you,'" he explains. His philosophy, borrowed from mentor, Wells CEO Richard Kovacevich, is more bottom up. "As CEO, my job is to support my direct reports in taking care of customers," he says.

Sohn's efforts to remake Hanmi in Wells' image have attracted curiosity, and a little skepticism, in the close-knit, hyper-competitive Korean-American banking community. The niche has been white-hot of late, with the four largest players-Hanmi, Wilshire Bancorp, Nara Bancorp and Center Financial-growing loans at an average annual rate of 29 percent over the past five years. Deposit levels have ballooned 24 percent per-year over the same period. Three of the four boast returns on equity in the 20 percent-plus range; Hanmi, at 14.4 percent is the laggard. (Wilshire Bancorp and Nara Bancorp were both named to USB's All-Star Banking Team this year for superior financial performance.) James Abbott, an analyst for Friedman, Billings, Ramsey Group, expects the banks, all publicly traded, to generate double-digit per-share earnings growth in each of the next two years, compared to around eight percent for the industry as a whole. And they'll continue to do it without the help of today's trendiest earnings-per-share-growth lever, the share buyback. "It's pure EPS growth, powered by strong revenues," he says.

"These banks have done phenomenally well over the past 10 years," adds Brett Rabatin, an analyst with FTN Midwest Research. "They're very efficient. They've grown tremendously, benefiting not only from growth in southern California's Korean community, but the region's economic expansion and real-estate boom. ... You don't see many banking segments that have done better."

Some explain away the banks' success as being in the right place at the right time. Southern California's commercial real-estate market has been sizzling, and the banks have taken advantage of the Fed's easy-money policies. "For the past six years, it's been a no-brainer," says

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Wun Hwa (Jack) Choi, CEO of Commonwealth Business Bank, a 2005 startup, and a former Hanmi chief credit officer. "You wake up every morning with more customers than the day before." If it were that easy, however, then all southern California banks would be flush with profits, which they're not.

A better explanation lies in the customer base and the banks' abilities to meet its needs. Koreans tend to be well-educated and entrepreneurial. New arrivals often come loaded with cash, which is good for the deposit base - about 25 percent of deposits are non-interest-bearing, double the industry average. They also pursue the American dream aggressively, often starting mom-and-pop retail shops or small manufacturing or import businesses. While English may not be their first language and they might struggle to understand the legal structure, they're in a hurry, and often need help. In fact, one of the most distinguishing features of the demographic, bankers agree, is just how impatient customers can be. They prize face-to-face service, and view waiting 10 minutes in a teller line as an affront. "Everybody thinks they are a VIP customer," Sohn says. "They want faster, better service, and will get very angry" if forced to wait.

The banks counter such demands with crisp efficiency and plenty of hand-holding. When faced with a surge of customers, it's not unusual to see everyone, including the branch manager, manning a teller station. All have Korean-speaking employees, who specialize in cutting the red tape of a new country, and offer referrals to attorneys, realtors and other trusted professionals. Choi encourages his bank's relationship managers to be "business consultants," partners who sometimes discourage clients from pursuing projects that don't make sense. That builds trust in a market that, even to folks who have been here for decades, can still feel foreign. "A lot of Koreans simply feel more comfortable going into a Korean-run bank," says Joe Gladue, an analyst with Cohen Bros. & Co. "It goes deep into the culture."

The banks specialize in loans that other institutions consider too dicey. A handful of big institutions-Bank of America, Wells and Washington Mutual among them-have leveraged their branch networks to capture Korean-American consumer business. Sohn estimates that mainstream banks hold about half of the segment's \$20 billion in deposits. But it's difficult for the big guys to fit a recent immigrant's business-loan request into a credit-scoring model, and other niches, such as Chinese-Americans, are larger. A Wells spokeswoman says that, "while the Korean market is interesting to us, it's not something we really focus on all that much."

Korean-American bankers gladly pick up the slack, relying mostly on their own backgrounds and know-how to underwrite such loans. "We interview them, talk about their plans, and based on our experience with these kinds of loans, we're able to make a decision fairly quickly," says Min Kim, CEO of \$2 billion-asset Nara. Adds Joanne Kim, chief lending officer for \$2 billion-asset Wilshire: "With our customers, if you only look at the papers, it might not look like a doable deal. But the old saying is true: Banking is a people business. When we go out and meet the customer, we often can find a way to underwrite the transaction."

It's a relatively simple business model, based mostly on relationships and word of mouth. Think of these institutions as community banks, with the "community" defined by ethnicity instead of geography. The banks may not be terribly sophisticated when it comes to technology or fee-based products, and the vast majority of their revenues come from the spread. The hand-holding allows the banks to capture loan yields about 1.5 percent higher than average, fueling strong margins. Expense control is another forte. Koreans are a thrifty people, Sohn explains, and the banks reflect that conservatism. Most have efficiency ratios in the 40 percent range, well below the industry average. They don't have a lot of branches, and the ones they do have are usually barebones operations, smaller than a mainstream bank office, and minus the granite and other fancy touches.

What the bankers lack in modern-day amenities they make up for with ambition and tenacity. Wilshire Boulevard, the bustling hub of Los Angeles' Koreatown-home to 40 percent of the 2.2 million Koreans in the U.S.-hosts some 15 Korean-American banks. While outwardly cordial with each other-Center hosts a well-attended annual golf tournament for executives and directors of the banks, for instance-competition for customers and employees is cutthroat. Sohn has lost workers to cross-town rivals, and to banks as far away as Atlanta. "There's nothing at all collegial about it. The competition is 10 times worse than at Wells Fargo," Sohn says, admitting he was initially taken aback by its intensity. "What worries me is that we're so busy fighting amongst ourselves that we could be weakening each other."

A spate of recent de novo launches hasn't helped. The space had five startups between 2004 and 2006. One newcomer went so far as to offer stock options to new teller hires, and others have raised the ante on deposit pricing. Until recently, some banks were offering retail CD rates that, at nearly 100 basis points above the industry average, exceeded wholesale funding costs. The startups "don't have any impetus to be profitable in the short term," Rabatin explains. "So they take their startup capital, leverage it up and throw crazy CD rates out there that everyone else feels compelled to match." Choi, whose Commonwealth is one of the newbies, notes that margins in the space, at about 4.5 percent, are still higher than industry averages, and argues that the larger banks should ignore the startups. The bigger Korean-American banks counter that they need to defend their turfs. Regulators recently placed a moratorium on the launching of new Korean-only banks. "If you want to start a bank today, it has to be multi-ethnic," Abbott says.

The competitive pressures have pushed the larger players into expansion mode. Most have loan-production offices in other cities with sizable Korean-American populations, such as Seattle and Denver. Nara has had branches in New York since 1998; Wilshire opened one in Dallas a few years ago, and last year paid \$16 million for Liberty Bank, a \$59 million-asset Korean-American institution in New York. They're also going multi-ethnic, chasing Indian, Iranian, Pakistani and Vietnamese customers. Already, more than 50 percent of both Hanmi's and Wilshire's loan portfolios come from non-Koreans. The needs of immigrant businesses are pretty much the same, regardless of country of origin, and many are intimidated by a mainstream bank setting. "Even if they're not Korean, we're all immigrants," Joanne Kim explains. "They have accents and so do I. That makes them much more comfortable talking about finances with us."

There are other challenges to overcome. Heavy volumes of trade finance and overseas wire transfers have regulators watching compliance issues closely. In recent years, the four big banks all have been slapped with memorandums of understanding by regulators for Bank Secrecy Act-related matters. Hanmi's came just months after Sohn arrived, and cost the bank hundreds of thousands of dollars in consultant fees, while delaying expansion plans. Before it was over, Hanmi had to double its compliance staff. Equally daunting is their reliance on real estate. At Hanmi, for instance, 65 percent of the loan portfolio is devoted to commercial real estate of one sort or another. For Wilshire, the tally is closer to 75 percent. Real estate continues to be strong in southern California, and the banks typically take sizable collateral positions. But if prices tank, the lending market could slump significantly. Several of the banks have strong Small Business Administration-origination operations, and all have been working to boost corporate and institutional loans. As with real estate, however, most of those loans tend to be variable rate, which has been good in a rising-rate environment, but could come back to bite if rates decline. "If rates drop, they're going to be exposed," Abbott says.

Sohn walked into this frenzied market with the cache of a rock star, perhaps the best-known Korean American, period. After a stint on President Nixon's Council of Economic Advisors, he joined old Norwest in Minneapolis, which in 1998 acquired Wells and took its name. He emerged as one of the most-quoted and accurate economists in the country, burnishing his Korean street cred with a regular column in Chosun, a big Seoul daily. When he hit Koreatown in 2005, expectations were unreasonably high. "We were hoping he would upgrade Korean banking to the next level," Joanne Kim says. The going has been slower than anticipated. Gradually, however, change is taking hold-at Hanmi, and to a lesser extent, the other institutions.

Sohn's broad goal is to transform Hanmi into a regional bank, a la Wells, with more products, a bigger footprint and a stronger sales culture. In some cases, he's experienced pushback. A new incentive structure, for instance, rewards individual accomplishment-a big departure from the typical Korean-American system where all workers get the same bonus. Competitors say some experienced bankers have jumped to rival institutions as a result. But he's also beefed up the product menu, with cash-management, wealth-management and leasing offerings, and plans to introduce mobile banking, already popular in Korea. Other banks are taking notice. Sohn says several have quietly inquired about his incentive plan. "We're hoping he'll do more of the things we don't do, so we can learn from him," Joanne Kim says.

In January, Hanmi acquired two insurance agencies, adding another cross-selling opportunity. More deals seem sure to follow, and other Korean-American banks are considered likely takeout targets. "If you're less than a \$10 billion bank, it's tough to say you're regional,"

Sohn says. One rumor matches Hanmi and Nara; another envisions a marriage with Center. Sohn predicts that the niche's big four will shrink to two over the next several years. Down the road, some analysts say Hanmi itself might make a nice prize for a bigger company-say, Wells. Sohn's too busy to think about that just now, though. "At Wells Fargo, I felt like I was always watching a very exciting parade. Here I get to lead it," he says-not only inside his bank, but across the niche. (c) 2007 U.S. Banker and SourceMedia, Inc. All Rights Reserved. <http://www.us-banker.com>
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