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Mutual of Omaha Doubles Down as Other Insurers Flee Banking

Mutual of Omaha Bank is settling into its role in the banking industry at a time when many insurers are running for the exits.

The banking arm of Mutual of Omaha had a splashy debut in 2007, swelling to nearly $7 billion in assets by leveraging its parent's financial strength to buy five banks in three years. It was among the first banks to take advantage of a failed-bank deal when the economy tanked.

Chief Executive Jeff Schmid is dedicated to digesting those deals and building a traditional community bank. After a fast start out the gate, he has shifted focus to a long-term goal of establishing good relations with regulators, building out technological capacities and making a name as a community-focused, relationship-based bank.

"In the early years we put a rocket ship on a covered wagon," Schmid says. "Now we're rebuilding it into a rocket sled that can stand the weight of a $7 billion bank."

Mutual of Omaha's plan to build a traditional community bank forms a sharp contrast with other insurer-owned banks, and may account for its staying power. While other insurance companies have rushed to leave the industry, Schmid says his bank's parent company remains committed.

"A lot of insurers looked at the relative size of their banking businesses and made the decision that it wasn't worth it," he says. "We're committed to the banking side of the business for the foreseeable future. Banking matters inside our company."

Insurers have staged a mass exodus from the industry in recent years. Since Mutual of Omaha Bank's debut, the number of insurance companies that own banks has dipped from around 40 to just a small handful now. Giants like MetLife, Allstate, Hartford Financial and Prudential have shed their charters in recent years.

Some insurers that bought banks as a temporary way to access emergency capital during the financial crisis divested them after the storm passed. Others sold to avoid being regulated like banks. MetLife CEO Steven Kandarian, for instance, has said that banking regulations don't allow his company to compete "on a level playing field" with other insurers, which are covered by a web of state-level regulations.

Another reason insurers have left is the uncertainty surrounding rules for nonbanks, particularly structurally important institutions, says Paul Newsome, an analyst at Sandler O'Neill.

"Those rules could eventually be more or less strict than the current insurance regulations," Newsome says. "But at the moment there are no rules."

SETTLING IN: "In the early years we put a rocket ship on a covered wagon," says Jeff Schmid, CEO of Mutual of Omaha Bank. "Now we're rebuilding it into a rocket sled that can stand the weight of $7 billion in assets.

Schmid, who was at American National Bank of Omaha for 18 years, spends much of his time building relationships with the Office of the Comptroller of the Currency, which became his primary regulator in 2011. Unlike many community bankers, particularly those working for insurers, he doesn't take issue with a heavy regulatory burden, which he sees as a necessary expense to make sure the industry plays fair.

"There was a time over the last 10 or 15 years where banks and bank leaders were not paying attention to the rules," he says. Banks now need to find ways to collaborate with Congress and regulators to determine which new rules work and which don't, he says.

Mutual of Omaha Doubles Down *continued*

Schmid's attitude toward regulation isn't the only thing that distinguishes his bank from other insurer-owned lenders. Many insurance companies merged with banks in the hope of cross-selling products, most famously Citigroup (NYSE: C) and Travelers in 1998. This model proved "overwhelmingly unsuccessful," says Meyer Shields, an insurance analyst at Keefe, Bruyette and Woods. "You can have good banks and you can have good insurance companies, but putting them together doesn't work."

Cross-selling is a much smaller part of Mutual of Omaha Bank's business, Schmid says. His main focus involves building a consistent culture across a far-flung network that comprises a dozen states from Hawaii to Florida. The failed-bank franchises, many of which had "tired and broken" cultures and processes, proved a particular challenge, he says.

"Growth creates a vacuum for talent and for strength of process and control, and I don't know if anybody's grown a $7 billion bank from scratch in six years," he says.

Schmid relies heavily on the parent company's resources. Mutual of Omaha made an initial investment of about $500 million. The bank also borrows expert personnel from the parent company for technical and risk-management processes, he says.

Building online offerings and mortgages are two key initiatives. Schmid admits that the bank's online services are "pretty basic," but he plans to invest up to $30 million over the next three to five years for improvements. Mutual of Omaha Bank also has a niche in lending to homeowners' associations, which Schmid calls the largest in the country.

It adds up to a profitable, consistent banking model. The bank earned $7.5 million in the first quarter and $38 million last year, with a 5.78% return on equity. Schmid's goal is to return 8% to 10% a year while growing organically at 5% to 8%. It has roughly achieved the growth goal since its last deal, in 2010.

Earnings pressure from the parent company exists, but less so than with huge, publicly traded insurers. Like State Farm, another insurer that has remained in banking, Mutual of Omaha is mutually owned by its policyholders, creating less pressure to turn an immediate profit than at a publicly traded company.

Mutually owned insurers are more concerned with providing long-term value and making customer relationships stickier, Shields says.

Schmid, too, is focused on the long term, including a huge initiative designed to figure out how to sell to a younger generation of customers.

"I focus most of my time on culture building and trying to understand my client, my future client," Schmid says.

by Chris Cumming