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PrivateBancorp Inc. Chairman Ralph Mandell, left, and Larry Richman, president and chief executive officer, in the company's soon-to-be headquarters on LaSalle Street, in the heart of Chicago's financial district. Richman said the physical move makes an important statement that the company is ready to dominate commercial banking in the middle market.

PrivateBancorp pushing forward with risky, ambitious growth plan

by Sarah Schaale
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Wealth manager PrivateBancorp Inc. is not-so-quietly nudging its way – both literally and figuratively – into middle-market commercial banking, and according to analysts, successfully so.

The Chicago-based financial services company's loans totaled \$5.1 billion in the first quarter, up 43 percent since the previous year and jumping from relatively flat loan growth in recent years. And although the company posted its second consecutive loss in the first quarter as a result of expensive recruitments, PrivateBank shares popped nearly 6 percent on earnings day and have continued to creep up ever since. Its stock is 11 percent higher than a year ago, the shares trading now between \$36 and \$38.

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Analysts are cautious, but most say PrivateBank's "strategic growth plan" – its launch pad to move the \$6 billion company into commercial banking – is promising.

"The plan is a challenge, but it is absolutely the right thing for them to do," said Peyton Green, an analyst at Cleveland-based FTN Midwest Securities Corp., an independent research firm. "It's certainly a revolutionary move in a lot of respects.

Changes brought on by the plan included hiring Arlington Heights resident Larry Richman to succeed Ralph Mandell (a co-founder of the bank who remains chairman of the board) as president and CEO, pushing loan growth out of the bank's commercial real estate comfort zone, adding new lending products, expanding its client base, and showering signing bonuses on 150 new employees, many of whom were lenders at LaSalle Bank until it was acquired last year by Bank of America.

Those bonuses totaled \$17.4 million in the last two quarters, equivalent to 46 percent of PrivateBank's net income of \$37.8 million in 2006.

"They bet a lot of money on it," said Dan Arnold, an analyst at New York-based brokerage Sandler O'Neill & Partners LP. "Critics will say they overpaid, proponents will say it was a smart move to take advantage of that opportunity."

"Most of the growth is coming from relationships they already had, which is a positive, because you don't want to see them growing just by forging new relationships just for the sake of growth."

At the onset of the plan, PrivateBank said it hopes to achieve 20 percent compound annual growth in its earnings per share over the next five years.

"The vision and opportunities are terrific," said Richman, one of many LaSalle recruits. "PrivateBank is a growth story."

Analysts expect the plan to keep PrivateBank in the red through 2008, with a consensus estimate compiled by Zack's Investment Research Inc. anticipating a loss of 21 cents per share. Yet PrivateBank shares get three buy ratings, eight holds and three sells.

Even Arnold, of Sandler O'Neill, who recently downgraded the stock to a sell after its recent rise, sees promise in the bank's growth plan.

"The first quarter [of 2008] confirmed that they're capable of growing at the rates that the most bullish people had hoped," Arnold said. "Long term, I do still like the story."

Before the plan, PrivateBank was enjoying long-running success, with double-digit growth in the last five years. Nevertheless, Richman said, the LaSalle acquisition showed PrivateBank's board of directors a "dislocation" in the market and an opportunity to diversify the company's products and expand its client base while retaining PrivateBank's grip on high-touch, relationship-driven banking.

“We want to be with the companies and individuals during their lifecycles,” Richman said. “It’s part of the theme of what we’re building at PrivateBank.”

PrivateBank was known in the Chicago area and beyond for catering to high net worth individuals and entrepreneurs and maintaining a loan portfolio around commercial real estate, Arnold said. The company’s 22 locations include offices in Chicago, suburban Cook County and three in DuPage and Kane counties. In April the company opened offices in Denver and Des Moines and announced its plan to move its headquarters to handsome former LaSalle Bank offices at 120 S. LaSalle St.

Arnold said PrivateBank will face competition from several banks, including JPMorgan Chase & Co., National City Corp. and Fifth Third Bancorp, along with Bank of America Corp. and regional banks such as First Midwest Bancorp Inc. and MB Financial Inc. LaSalle dominated commercial middle-market lending, and its acquisition left a gap that PrivateBank is moving to fill.

The plan is a deviation from a more traditional growth strategy of acquiring another bank. Analysts say the inside, organic approach is a smarter move and plays more favorably to PrivateBank.

David Long, an analyst at William Blair & Co. LLC, said PrivateBank’s plan is more cost-effective, and allowed the company to maintain control of its balance sheet. Green at FTN Midwest said PrivateBank is reaping the benefits but avoiding the risk that comes with an acquisition.

“It’s a concept our investors understand,” Richman said. “We’re investing in them and they’re investing in us. If you can do it organically, it’s much more predictable and sustainable.”

Nevertheless, Arnold observes, PrivateBank faces the task of meshing LaSalle folks into PrivateBank, which he says gives its bankers a fair amount of autonomy. “It’s tough from an ego standpoint,” Arnold said. “Some of these people that were top dogs are going to be playing second fiddle to these LaSalle guys that came in.”

Richman says blending the two cultures will come over time.

“It’s never easy, but it’s something we’re very focused on,” he said. “It’s a collegial culture, and everyone has the ‘one bank, one team’ mentality.”

“If they are able to execute everything they say they can,” Arnold said, “it will go down as a great strategic move. But if not, expenses will be very high.”