Finding Your Niche: The Independent School Banking Division

Establishing and Scaling a High-Performing Market Vertical
Within a Full-Service Commercial Bank

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Executive Summary

Founded in 2005 by former luxury home builder Frank Sorrentino III and a group of local investors, ConnectOne Bank (hereinafter "CNOB" or the "Bank") is a full-service commercial bank headquartered in Englewood Cliffs, NJ with approximately $9B+ in total assets. Guided by a set of established core values, employees are tasked with maintaining a culture of placing "People First" in all their respective interactions; both internal and external. These core values have shaped the way in which all client relationships are handled and subsequently reinforce ConnectOne Bank's reputation as a market leader in delivering exceptional products and services.

Utilizing both organic growth and strategic institutional acquisitions, ConnectOne Bank has positioned itself as a major player in the New York City Metropolitan Area and beyond. Utilizing an intentional branch-lite operating model with twenty-four (24) branches spanning New York to South Florida, the Bank continues to favor investments in new technologies to drive innovation over a robust physical branch presence. As such, ConnectOne Bank operates in an extremely efficient manner compared to peer institutions and it remains the opinion of Management that embracing the evolution of digital financial services and adopting new technologies is necessary in order to stand out in a crowded industry. By partnering with various financial technology (FinTech) companies whose product and service offerings are complementary to ConnectOne Bank's mission of providing superior client service, Management believes that rapid future growth and profitability is both attainable and expected.

In addition to ConnectOne Bank's approach of adopting new technologies and driving innovation to better serve its client base, the Bank has also responded to a greater demand for dedicated groups or teams within the organization who are committed to working specifically with clientele in certain industries or "niche" market verticals. Taking advantage of blind spots which may exist at other institutions, ConnectOne Bank works strategically to seize opportunities by building and empowering specialized groups within the Bank whose team members serve as subject matter experts for a particular line of business. Examples of such existing groups include ConnectOne Bank's Healthcare Banking and Franchise Banking Divisions.

The purpose and focus of the subject proposed initiative is the build-out of a distinct "niche" market vertical within the Bank to be known as the Independent School Banking Division (hereinafter 'ISBD" or the "Division"). Specifically working to target and win the banking relationships of independent pre-kindergarten through grade twelve schools and certain higher educational institutions, the Division will seek to establish long-term, mutually beneficial borrowing and deposit relationships with these institutions. With each school governed by a volunteer elected Boards of Trustees and managed by various administrative staff and business officers, these institutions are unique in that they charge established tuition rates and fees for attendance rather than relying on government funding for operations. These schools utilize a seasonal cash flow model whereby tuition and fees (largest sources of revenue) are collected at specific points in time during the school's fiscal year, with expenses recognized continuously over that same year. With a reputation for being notoriously exclusive, the schools competing for market share i.e., student enrollment must ensure that their programming and facilities are state-of-the-art and free of deferred maintenance so as to attract and enroll new students year-over-year.

This is where the Independent School Banking Division comes in. Serving as subject matter experts in both structuring debt financing and deposit account relationships, members of the Independent School Banking Division will seek to act in an advisory capacity to potential school clients by helping them understand the nuances of various financing arrangements available to them and subsequently work to tailor solutions that meet the needs of a particular school. Often requesting large, long-term credit facilities (most notably tax-exempt bond issuances), it will be the responsibility of the Independent School Banking Division to understand and analyze these credit requests in order to make responsible recommendations that work for both the school and the Bank from a cash flow perspective.

Business development efforts will be specifically designed around prospective clientele so that team members can engage in quality and effective outreach. Second to the personnel expense, this area of the initiative will require the largest financial investment as team members will need to travel to attend various industry conferences, school-based fundraising events and other types of exhibitions deemed valuable in garnering new business. From both relationship and financial perspectives, scaling the Independent School Banking Division's portfolio will benefit the Bank in many ways. As is currently demonstrated with the rapid growth and success of CNOB's Healthcare and Franchise Banking verticals, the Independent School Division will also attract high-quality institutional clients, many of which are hundreds of years old and exceptionally financially sound. Often possessing impressive balance sheets and significant revenue generation, these institutions are known to possess extensive liquidity in the form of cash, cash equivalents and investments (Endowment funds) as well as valuable fixed assets which often include the real estate or campuses owned by the school. This financial strength allows many schools to take on sizeable debt, often in amounts of multi-millions of dollars which are used for a variety of purposes including but not limited to capital improvements or new construction, campus expansions or deferred maintenance projects. Furthermore, significant cash balances (often eight to nine figures) maintained by school borrowers will ultimately become CNOB deposits and work to significantly offset the Bank's cost of funds relative to the various credit facilities extended to these schools. The result is a durable and desirable niche portfolio with a deposit-to-loan ratio superior to most other lines of business.

The financial investments included in this initiative combined with the implementation of various processes as outlined herein should ultimately result in increased productivity and overall profitability, while also maintaining favorable portfolio metrics and high credit standards. In clearly defining and formalizing the roles of team members who will be dedicated to furthering the group's efforts, the Division should experience a steady increase in new client acquisitions. As these team members are successfully trained and deemed self-sufficient in their roles, ongoing communication, training, and strategic portfolio management/maintenance will prove critical to the future growth and success of the Division. The primary value proposition of the subject initiative lies in the complementary nature of the Division's endeavors to the culture and growth strategy of CNOB as a whole. Encouraged to employ an entrepreneurial approach in all client interactions, team members will take ownership of their efforts in order to position the Bank as a leading service provider within the independent school industry. With the commitment and support of Executive Management, and the Bank's continued investments in cutting-edge financial technology, the Independent School Banking Division will be empowered to seek out quality opportunities spanning an extensive geographic footprint resulting in greater value creation for the Bank and its Shareholders. As the proposed initiative outlined herein should substantiate, the establishment of a specialized group within the Bank dedicated to working solely with independent schools is undoubtedly a worthwhile investment that if implemented will align with the Bank's risk appetite and support future growth in a significant way. It is for these reasons that the Project Leader (Writer) respectfully recommends the review and subsequent approval of the proposed strategic initiative that is establishing the Independent School Banking Division.

Part I: Introduction and Background

History and Overview of ConnectOne Bank's Business Model

ConnectOne Bancorp, Inc. operates as the bank holding company for ConnectOne Bank (hereinafter "CNOB" or the "Bank"), a state chartered, commercial bank headquartered in Englewood Cliffs, NJ. ConnectOne Bank offers a full suite of deposit and lending products and services with a focus on small to midsize businesses, local professionals, and individuals. With a strategic, limited brick-and-mortar presence consisting of twenty-four (24) branch locations spanning New Jersey (15), New York State (8) and South Florida (1), the Bank continues to strategically position itself within markets that present opportunities because of large and growing populations, depth of the local real estate markets, access to small, middle market and large businesses, and an abundance of wealth[1]. As of September of 2022, ConnectOne Bank reports total assets of $8.8B, and a market capitalization now exceeding $1.0B.

Founded in 2005 by local luxury homebuilder Frank Sorrentino III and a group of local investors, ConnectOne Bank initially operated as North Jersey Community Bank (NJCB). Dissatisfied with his personal experience in dealing with area banks, Mr. Sorrentino recognized an opportunity to significantly improve the client experience within the commercial banking industry. At a point in time where industry-wide M&A activity and high employee turnover resulted in friction and frustration for many clients of local banks, Mr. Sorrentino established a new institution where the primary goal of placing *"People First"* would remain paramount. This guiding principle would apply to clients and employees alike, ultimately shaping CNOB's reputation as a growth-driven firm. Through company-wide employee input and the creation of a formal Culture Committee, CNOB cemented a set of core values which employees consistently implement to make sound decisions and remain aligned with the Bank's mission. These five central core values consist of **People First, Sense of Urgency, We Connect, Make an Impact and**

[1] https://www.connectonebank.com/OurLocations

Forward Thinking (Appendix A: ConnectOne Bank's Core Values). The Bank's interdepartmental collaboration has been crucial in developing CNOB's company culture and ultimately its ability to provide stand-out service in a crowded New York Metropolitan Area market. As a result, CNOB's slogan remains *"a better place to be."*

As stated by Executive Management in CNOB's Annual Report Form 10-K dated December 31, 2021[2], "Our business model includes using industry best practices for community banks, including personalized service, state-of-the-art technology, and extended hours. We believe that this will generate deposit accounts with somewhat larger average balances than are found at many other financial institutions. We also use pricing techniques in our efforts to attract banking relationships having larger than average balances."

ConnectOne Bank Leadership and Personnel

With growth comes opportunity. Understanding that great leadership must start from the top of an organization, CNOB has built a talented and diverse Board of Directors and Executive Management Team. The attached chart is a current listing of the Banks's Executive Management Team which includes eight Executive Officers (Appendix B: Executive Management Team Hierarchy). Firmly believing that employees are the Bank's greatest assets, leadership empowers team members to make sound business decisions quickly by providing them the tools and technology needed to exceed client expectations. CNOB's high quality personnel, currently approaching five hundred (500) full-time employees, is encouraged to be bold and take an entrepreneurial approach in their efforts to identify and execute on opportunities to succeed within their respective roles. As a result of this encouragement and support, Management is often able to fill newly created or open positions by way of promoting existing personnel

[2] https://d18rn0p25nwr6d.cloudfront.net/CIK-0000712771/d8adc721-3593-4535-a0da-4115a4d742bb.html

from within the organization. Case in point; the Project Leader's (Writer) current role with the Bank is that of Vice President (VP), Commercial Loan Officer. Serving in various roles over a twelve-year tenure, the Project Leader now reports directly to the First Senior Vice President (FSVP), Business Development Team Leader. The Project Leader is tasked with both sourcing new business to drive profitability as well as managing a significant existing portfolio inclusive of large commercial credit facilities and deposit relationships. For the purpose of this Strategic Capstone Project, the Project Leader will work directly with the FSVP and other designated Bank officers and employees as necessary to lead the development and implementation of the proposed organizational enhancements outlined in this initiative.

Strategic Growth and Dynamic Expansion

In February of 2014, in efforts to align the Bank's brand with a vision of growth and expansion, NJCB rebranded as ConnectOne Bank (CNOB). Shortly thereafter, CNOB went on to raise capital in excess of $50MM as a result of an Initial Public Offering (IPO). The IPO was the first for a New Jersey-based bank in over ten (10) years and represented strategic action taken by management to set the stage for future growth and development. ConnectOne Bancorp, Inc. currently trades on the NASDAQ Exchange (NASDAQ: CNOB).

In addition to CNOB's organic growth since inception, the Bank has also utilized strategic institutional M&A to bolster its presence and expand into complementary markets to strengthen the Bank's operating performance and financial position. Five notable milestones accomplished over the Bank's fairly short history which demonstrate this strategy in action are outlined as follows:

- In July of 2014, ConnectOne Bancorp, Inc. successfully executed a merger of equals with Center Bancorp, Inc., the bank holding company for Union, NJ based Union Center National Bank (UCNB).

This merger significantly increased CNOB's branch network and financial position to $3B+ in total assets.

- In January of 2019, Connectone Bancorp, Inc. completed a second institutional merger with Hudson Valley, NY based Greater Hudson Bank. Greater Hudson held $402MM in deposits and $341MM in loans giving the combined banks total assets of $5.7B. The acquisition was considered strategic in that deposit-heavy Greater Hudson Bank further enhances CNOB's impressive loan growth and diversification.
- In June of 2019, ConnectOne Bancorp, Inc. successfully completed the strategic acquisition of online business lending platform BoeFly, Inc. Operating out of its offices in Boston, MA and New York, NY, BoeFly is an online lending marketplace that serves and connects (primarily) small businesses and franchises with lenders and loan brokers on a national level. This acquisition was viewed by CNOB as an opportunity to further diversify its revenue streams as well as demonstrate its willingness to partner with financial technology companies. In remaining proactive and forward thinking, CNOB has continued to embrace emerging technologies and collaborate with Financial Technology (Fintech) firms rather than solely compete with them.
- In January of 2020, ConnectOne Bancorp, Inc. completed its acquisition of Bancorp of New Jersey, Inc., parent of Bank of New Jersey. This strategic acquisition provided enhanced scale and additional growth opportunities for CNOB within its current market. Bank of New Jersey added approximately $800MM in deposits and loans to CNOB with the transaction intended to create long-term value for shareholders and increase the scarcity value of CNOB's franchise.
- Completed in September of 2022, the Bank's most recent strategic initiative saw CNOB formally open its first physical office in Florida, located in West Palm Beach. What could initially be considered a reactionary decision to follow the significant migration of existing clientele to South

Florida during the COVID-19 pandemic evolved into the investment and development of a robust team of experienced Bankers who are utilizing CNOB's technology, infrastructure, and access to key decision makers to move quickly and seize opportunities within a market of incredible wealth and growth potential.

As depicted in ConnectOne Bancorp Inc.'s Form 8-K dated September 7, 2022[3], the following illustrations summarize Management identified competitive advantages in relation to future organic growth and dynamic expansion:

[3] https://d18rn0p25nwr6d.cloudfront.net/CIK-0000712771/fb26d322-4da6-44ba-818e-7d18d95ab70a.html

Organic Growth

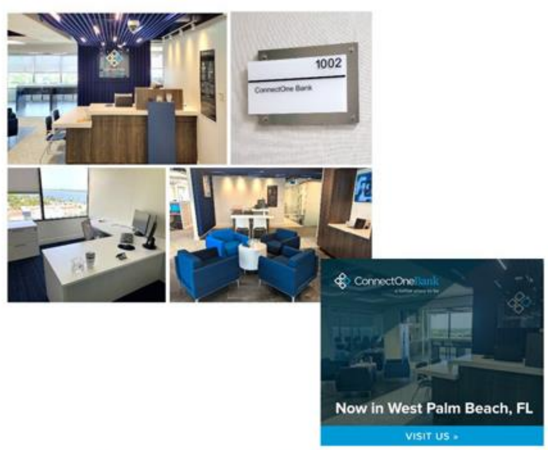
Opportunities to expand as a result of post-pandemic trends

- Densely populated, lucrative markets
- Strong demand for personalized service among small to mid-sized business owners
- Our target market is largely dominated by the largest institutions in the country, leaving tremendous opportunity for banks catering to middle market businesses
- Diverse economy provides numerous avenues for revenue expansion, while also remaining resilient during severe economic downturns

Dynamic Expansion

Leveraging technology to drive new opportunities

- Roots in NY/NJ metro area allow the bank to expand with clients as they build out-of-state outposts
- Digital investments coupled with ability to attract top talent allows for dynamic expansion
- Banking Hub model allows ConnectOne to expand in a nimble way
- Relationship-focused model has proven to be a clear differentiator across markets



Expansion into South Florida

- New office in West Palm Beach, FL supports clients' growth
- Team of 8
- Organic growth accelerating
- Loan origination in excess of $200MM by year end

Financial Condition

As reported and published by S&P Global Market Intelligence[4], the following chart highlights CNOB's strong financial position at periods ending 09/30/2022 and 12/31/2021:

Period Ended	2022 FQ3 YTD 09/30/2022	2021 FY 12/31/2021
Balance Sheet ($000)		
Total Assets	9,478,252	8,129,480
Total Net Loans	7,816,813	6,750,099
Total Deposits	7,310,510	6,332,953
Equity Attributable to Parent Company	1,148,295	1,124,212
Total Equity	1,148,295	1,124,212
COVID-19 Financial Disclosure		
Paycheck Protection Program Loan	11,458	93,057
PPP Loan Ratio	0.15	1.38
COVID-19 Loan Modification	N/A	500
COVID-19 Loan Modification Ratio	N/A	0.01
Processing Fees on PPP Loans	N/A	9,500

Balance Sheet Ratios (%)		
Loans/ Deposits	108.07	107.83
Securities/ Assets	7.22	7.09
Total Equity/ Total Assets	12.12	13.83
Tangible Equity/ Tangible Assets	10.06	11.46
Tang Common Equity/ Tang Assets	8.87	10.06

Since inception in 2005, Management and Stakeholders have recognized operational efficiency as a crucial component of the Bank's growth, innovation, and success. The efficiency ratio is an important

[4] https://ir.connectonebank.com/financial-information/financial-highlights/default.aspx

metric used in determining a bank's ability to convert resources into revenue and measures the cost of producing a dollar of revenue, net of financing costs. Maintaining superior efficiency ratios below 40% relative to its peer institutions year-over-year, CNOB prides itself on providing best-in-class client service while operating with a lean staff and a limited, yet strategic brick-and-mortar presence. Recognized as one of the most efficient banks in the country, CNOB has demonstrated consistent execution of strategic priorities to remain well positioned for success. Further reported and published by S&P Global Market Intelligence[5], the chart below includes key measures of CNOB's performance, profitability and efficiency which have remained robust over the periods ending 09/30/2022 and 12/31/2021:

Period Ended	2022 FQ3 YTD 09/30/2022	2021 FY 12/31/2021
Profitability (%)		
Net Income	92,654	130,353
Net Income Attributable to Parent	92,654	130,353
ROAA	1.45	1.69
Core ROAA	1.50	1.70
ROAE	10.79	12.94
ROATCE	14.50	17.37
Core ROAE	11.17	13.06
Net Interest Margin	3.75	3.66
Reported: Net Interest Margin	3.76	3.66
Efficiency Ratio	38.09	38.25
Noninterest Inc/ Operating Rev	4.75	5.46

[5] https://ir.connectonebank.com/financial-information/financial-highlights/default.aspx

As stated in ConnectOne Bank's 12/31/2019 Annual Report[6], "maintaining a solid capital foundation is a primary goal of the Bank. As such, the objective with respect to the capital planning process is to effectively balance the retention of capital to support future growth with the goal of providing stockholders with an attractive long-term return on their investment." As reported by the Bank and published by S&P Global Market Intelligence[7], the chart below includes measures of CNOB's Capital Adequacy position at periods ending 09/30/2022 and 12/31/2021:

Period Ended	2022 FQ3 YTD 09/30/2022	2021 FY 12/31/2021
Capital Adequacy		
Tier 1 Common Capital (CET1)	854,158	793,495
Tier 1 Capital	970,240	909,577
Tier 2 Capital	240,505	228,773
Total Capital	1,210,745	1,138,350
Total Risk-weighted Assets	8,374,098	7,458,850
Tier 1 Common Capital (CET1) Ratio	10.20	10.64
Tier 1 Ratio	11.58	12.19
Total Capital Ratio	14.45	15.26
Liquidity Coverage Ratio	N/A	N/A
Leverage Ratio	10.95	11.65
Basel III Leverage Ratio	N/A	N/A

[6] https://s26.q4cdn.com/569618751/files/doc_financials/2019/ar/2019-AR.pdf
[7] https://ir.connectonebank.com/financial-information/financial-highlights/default.aspx

Market Analysis and Competition

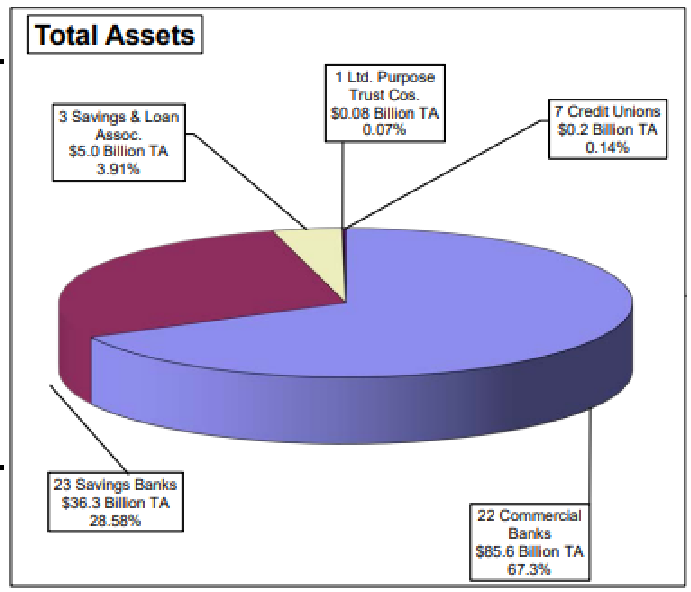
ConnectOne Bank operates primarily within the New York-Newark-Jersey City, NY-NJ-PA Metropolitan Statistical Area (MSA). Home to approximately 6% of the U.S. population, the New York Metropolitan Area remains the most populous in the U.S. by a significant margin spanning approximately 6,685 square miles with a population of 19.7 million residents (median age of 39.5). Serving as an epicenter for numerous industries including finance, international trade, news/media, real estate, education, fashion, entertainment, tourism, the New York Metropolitan Area is one of the most important and influential economic regions in the World. The economy of the New York-Newark-Jersey City, NY-NJ-PA MSA employs 9.69 million people with the largest industry employers being health care and social assistance (1,579,040 people), educational services (1,001,077 people), and professional scientific and technical services (935,497 people). The highest paying industries are finance and insurance ($102,163 average income), utilities ($90,451 average income), and finance and real estate ($90,451 average income). According to Census Reporter, households within this MSA reported median annual income of $84,409; greater than the median annual income of $69,717 across the entire U.S. by a wide margin of 20%[8].

While opportunity is extensive in this market, competition from other institutions also remains aggressive within this landscape. ConnectOne Bank's diverse and experienced leadership team thoroughly understands the highly competitive nature of the banking industry. Facing immediate and future competition both in deposit gathering and loan origination, CNOB competes with numerous commercial and savings banks along with loan associations; many of which have larger asset bases and capital/lending limits. As reported by the Federal Deposit Insurance Corporation (FDIC), CNOB maintained a modest 1.27% of the total New Jersey market share as of June 30, 2022; with the top three

[8] https://censusreporter.org/profiles/31000US35620-new-york-newark-jersey-city-ny-nj-pa-metro-area/

spots belonging to Bank of America with 17.20%, TD Bank with 13.43% and Wells Fargo with 10.55% *(Appendix C: FDIC-Insured Institutions Deposit Market Share Report as of June 30, 2022)*. According to New Jersey Financial Institution Statistics compiled by the State of New Jersey Department of Banking & Insurance as of December 31, 2021, the competition for market share includes a diverse range of institutions from local community banks with total assets of less than $1.0B to large money center institutions. As shown in following chart, competition in the New Jersey market is currently comprised of fifty-six financial institutions with combined total assets exceeding $127B:

Institutions By Charter Type	**Total Assets** *(000s of Dollars)*
Commercial Banks 22	85,615,089
Savings Banks 23	36,346,291
Savings & Loan Assoc. (S&Ls) 3	4,971,133
Limited Purpose Trust Cos. (LPTs) 1	82,852
Credit Unions 7	180,662
56	**127,196,027**



*** Includes Commercial Banks, Savings Banks, Savings and Loan Associations, Limited Purpose Trust Companies, and Credit Unions**

While CNOB has historically faced stiff competition from larger New Jersey-based banks such as Citizens Bank, Lakeland Bank, Valley National Bank and Provident Bank, recent significant M&A activity within the local New Jersey market has proven beneficial to ConnectOne Bank in terms of both its new client and talent acquisition efforts. As these newly formed institutions enjoy immediate growth in market share, CNOB works to take advantage of blind spots and seize opportunities to further build upon its robust offerings and deliver an amazing client experience.

In addition to traditional institutions, the banking industry at-large has begun to face stiff competition for deposit, credit and money management products from non-bank technology firms, or Fintech companies, which may offer products independently or through strategic relationships with insured depository institutions. Despite this fierce competition and current market volatility, CNOB is well positioned for success. In maintaining a high-quality loan portfolio and employing prudent expense management, the Bank intends to remain extremely efficient by industry standards. Despite recent macroeconomic uncertainty and market volatility, CNOB remains well capitalized and prepared to not only endure but embrace future changes in both the economic and technological landscapes. From a financial perspective, historical year-over-year widening of the Bank's Net Interest Margin (NIM) provides Management with confidence that the Bank will continue to experience growth, increased profitability, and shareholder value.

Part II: Strategy and Implementation

Recognizing Opportunity and Capitalizing on Change: The Niche Market Vertical

Change is constant. Financial institutions must evolve in-line with their target markets as business operating models and enhancements in technology are implemented by existing and prospective clients and competitors. In broadly analyzing the current business banking landscape, it is apparent there has been a substantial transformation over the past decade. Both advances in technology and tighter government oversight have contributed to the emergence of a new reality and way of conducting business. The needs of entities have become more convoluted, which necessitates a higher degree of service and understanding than was ever required in the past. Because of this, banks can now specialize in specific market sectors, enabling them to provide a more personal and comprehensive service level for their clients. As a direct result, CNOB has determined that a very effective method for attaining the reputation of an industry standard bearer in banking services is to concentrate its efforts on tailoring products and services to attract a specific clientele.

With the overall objective of CNOB being asset growth by way of client acquisition, the Bank continues to capitalize on opportunities which come as a result of market disruption; both in the form of traditional institutional M&A activity and the adoption of new technologies. CNOB's ability to respond to change has led to success in attracting superior revenue generating talent from other institutions, with the Bank continuing to evolve and garner new clients who have been displaced by transactions; creating opportunity for CNOB to accelerate organic growth. The addition of new talent possessing in-depth knowledge of specialized "niche" market verticals allows the Bank to expand its reach, targeting both new loan and deposit-focused business lines. Examples of recent niche market verticals that CNOB has been focusing and building upon are the Healthcare and Franchise Banking verticals. While new ventures for the Bank, CNOB's ability to recognize opportunity, make informed investments and deploy resources as necessary to create greater value through highly efficient, scalable platforms focused on providing unparalleled service to the select client base. With the recent expansion of the Bank's footprint down to South Florida, there is an enhanced ability for Banker's to attract and retain long-term, quality deposit relationships leading to accelerated growth and profitability for CNOB and its Shareholders. As Chairman and CEO Frank Sorrentino III stated in an article entitled *"The Future of Business Banking: Fintech Innovation + Human Advice,"* published by The Financial Brand in June of 2022[9], *"Today, community is defined more by the type of business you are in than by metropolitan area."*

[9] https://thefinancialbrand.com/news/business-banking/the-future-of-business-banking-fintech-innovation-human-advice-147446/

Utilizing an approach outside the scope of traditional and often broad Bank profitability measures, these initiatives will consider specific metrics associated with the subject niche vertical included but not limited to areas such as fee income, deposit-to-loan (and vice versa) ratios and portfolio cash deposit balances. As with both the Healthcare and Franchise verticals, CNOB has employed a hybrid approach utilizing both new outside talent acquisition and the elevation of existing employees who are familiar with the Bank's systems and technology. To date, these verticals have gained momentum and continue to grow at a rapid pace as the Bank both works to tailor its products and services to meet the specific needs of these clients as well as partner with various FinTech companies who provide complimentary services and technology to these business lines.

<u>Case for The Independent School Banking Division</u>

The purpose of this Strategic Capstone Project initiative is to concentrate, enhance and further build out the specific CNOB niche market vertical; the Independent School Banking Division (hereinafter the "ISBD" or "Division"). This Division's target clientele consists of independent pre-kindergarten through grade twelve educational institutions; sometimes referred to as "Private" schools. These independent schools charge tuition fees to attend instead of being funded by the government. These schools do not follow a national or state educational curriculum. Independent schools are most often established as non-profit or not-for-profit corporations or organizations with 501(c)(3) designations under the U.S. Federal Tax Code. That said, they are still expected to operate and be governed in a manner akin to for-profit corporations, with significant fiduciary duties and decisions resting on the shoulders of an elected Board of Trustees and various Administrators of these institutions. While these schools are mission-based institutions which exist for the purpose of education and community, tuition rates often exceed $50,000 per student on an annual basis, with ongoing levels of annual giving and financial support often expected from attending families. As such, the independent school industry at-large presents a high financial barrier of entry that has arguably out-priced the middle and lower-income earning households in their respective geographic areas; an exception being certain attending families who qualify for financial aid awards due to a school's pursuit of achieving socioeconomic diversity, equity and inclusion within its student body and community. Revenue is generally derived from tuition fees and giving, both annual giving and planned Capital Campaign contributions to fund campus improvements, while annual operating expenses generally remain consistent year-over-year. From a balance sheet perspective, more established schools may possess endowments with values exceeding $10MM+ and operating cash balances of $1MM+, with total debt to total net asset ratios of less than 1.0:1.0.

CNOB currently maintains a noteworthy portfolio of independent school client relationships, including those of both borrowing and non-borrowing natures. As the Bank has realized in its acquisition of these independent school relationships to date, this vertical often consists of robust, long-term banking relationships. As outlined in CNOB's core values; the ability to be bold and feel empowered to make sound decisions quickly will work in favor of the ISBD and should be met with the same enthusiasm and support that is offered to any other market vertical or internal business development teams within the Bank. Utilizing a collaborative approach, designated members of the ISDB will continue to work with Executive Management and other internal teams to seize opportunities to grow the portfolio while appropriately managing risk and maintaining high credit quality standards. Working with existing subject matter experts, new future team members will be formally trained and exposed to various educational resources including hands-on credit and cash management training taught by experienced Bankers within the ISBD and the larger CNOB organization.

The Strategic Fit

The independent school sector's status as an attractive target for CNOB is the result of numerous factors. To start, independent schools maintain a considerable demand for financial services, including both credit and non-credit. This requirement includes a wide variety of financial options. For example, to perform capital projects which can involve constructing new buildings or improving existing ones, schools often utilize large bank financings. Additionally, and potentially most importantly, independent schools and their business officers are known for their strong emphasis on personal relationships, a trait that aligns with CNOB's aim to provide its clients with an elevated level of relationship-based service. In line with CNOB's core value of "move fast and get things done," the ISBD will work to deeply understand the independent school industry as a market segment and have access to key decisions makers in the Bank from which the Division is able to garner buy-in or not for a given opportunity in an expedited manner.

While one specific School's philosophy, teaching approach and student enrollment differs from the next, certain metrics of success (or failure) remain similar and measurable. For example, the total annual net tuition revenue that a school earns, typically the school's largest and most consistent source of revenue driven by student enrollment, should ideally be significant enough to cover the operating expenditures that the school incurs over its fiscal year. If a school is not producing year-over-year operating surpluses, it may very well end up eroding its liquidity over time as it resorts to utilizing resources from its balance sheet to fund operations. While this may be an oversimplified example or a "tip of the iceberg" assessment in determining whether a school thrives, survives, or ultimately fails, it begins the conversation around determining a school's financial needs and goals; further amplifying the significance of having a banking partner who understands how to help them achieve those.

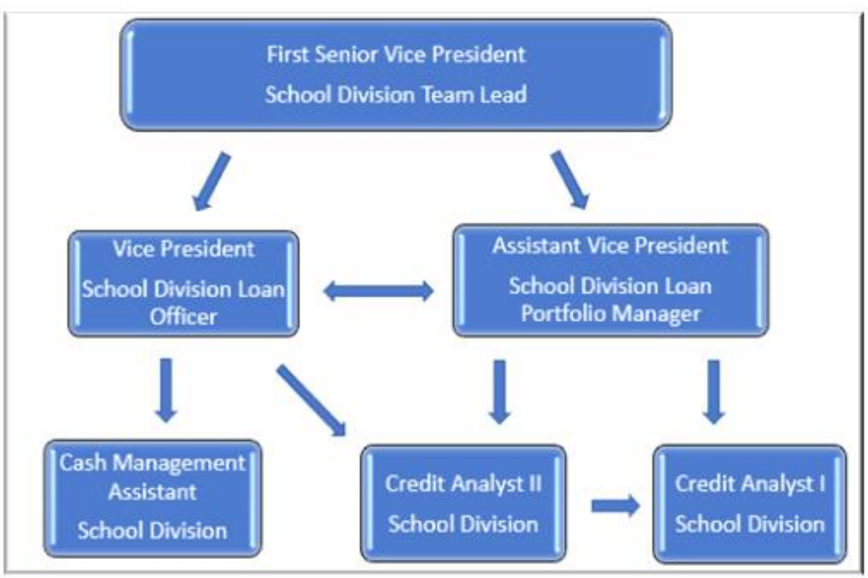
From both relationship and financial perspectives, scaling the Independent School Banking Division's portfolio will continue to benefit the Bank in many ways. As is currently demonstrated with CNOB's Healthcare and Franchise Lending verticals, the ISBD will attract high quality institutional clients, many of which are hundreds of years old and financially sound. Often possessing impressive balance sheets and high revenue generation, these institutions are known to possess extensive liquidity in the form of cash, cash equivalents and investments (endowment fund) as well as significant fixed assets which often include the real estate/campuses owned by the schools. This classifies many schools as high-quality candidates for large loan borrowings, often in dollar amounts of multi-millions which are utilized for various purposes including capital improvements or construction, campus expansions or deferred maintenance projects. Furthermore, the significant cash balances (often eight to nine figures) held by schools ultimately become deposits at the Bank, which then work to significantly offset the cost of funds for the various credit facilities extended to the schools. The result is a durable and desirable deposit-to-loan ratio superior to other types of borrowers/lines of business.

<u>Alignment and Designation of Team Members</u>

The alignment and designation of both new and existing employees will be required to successfully implement this initiative. As such, the ISBD will utilize both external talent acquisition and the internal appointment/promotion of existing employees where appropriate in efforts to minimize the learning curve and time spent on new employee onboarding and systems/job function training. The Project Leader (Writer), who currently holds the position of Vice President, School Division/Commercial Loan Officer, will be actively involved in the designation of team member job functions and delegation of various tasks that fall under the ISBD's purview. The team will then actively collaborate to measure growth and success by tracking loan and deposit balance growth (or loss) over each quarter, various fee income earned, and other key metrics utilized by designated Bank Officers/Independent School Banking Division team members. In order to ensure all functions of the Division are carried out successfully, the ISBD will require an initial minimum of six (6) full-time employees. Various functions of the Division include client-facing business development and sourcing, loan underwriting and portfolio management, deposit account opening/funding, setup and implementation of online banking and cash management services. The proposed structure of the Division includes the following:

- **FSVP, School Division Team Lead (Department Head)**
- **VP, School Division Loan Officer (Project Leader)**
- **AVP, School Division Loan Portfolio Manager**
- **School Division Credit Analyst(s) I and II**
- **School Division Cash Management Assistant**

The Independent School Banking Division's hierarchy will flow as illustrated in the following chart with the FSVP, School Division Team Lead reporting directly to Executive Management:



ISBD team members will also collaborate with dedicated internal Cash Management and Retail Banking Partners to fully understand and manage the entirety of the [often sizable] school client relationships. Further development of these internal relationships will also provide additional opportunities for the Bank to increase income by expanding on existing relationships. The Division will establish routines so as to have productive ongoing discussions around efforts and results, both successes and failures**.**

Implementation Plan and Considerations for the Future

In her article published on Score's website in July of 2019[10], author Anita Campbell succinctly describes scalability stating that *"Scaling a business means setting the stage to enable and support growth in your company. It means having the ability to grow without being hampered. It requires planning, some funding, and the right systems, staff, processes, technology, and partners.*" The inclusion of this excerpt felt appropriate and relevant as the culture at CNOB bears similar traits. While "culture" has become a highly important aspect of any company's make-up and reputation, Ms. Campbell further suggests that when given the right tools and a healthy amount of freedom and empowerment, great things can happen. It is in this entrepreneurial spirit that the ISBD will operate. For example, the ISBD must formulate a strategy for the business development and sales activities of the newly formed division. This would involve both traditional and digital marketing approaches; examples being attending industry events and webinars to spread knowledge of the ISBD's existence to prospective school clientele. The ISBD will function as a specialized team of subject matter experts within CNOB, with a dedicated team of Bankers and personnel in support roles. The goal of establishing, tracking and appropriately reporting quantifiable metrics within the ISBD will require that these team members formalize, visualize, and

[10] https://www.score.org/resource/blog-post/how-scale-business#:~:text=Scaling%20a%20business%20means%20setting,processes%2C%20technology%2C%20and%20partners.

inspire further buy-in and investments in various areas such as human resources to grow in-kind with further client acquisition and exceed expectations (CNOB Core Values). The ISBD will utilize human, financial and technological resources within the Bank to develop a full array of deposit and loan products that meet the client needs rather than utilizing a "one size fits all" sales approach. This includes drafting and implementing industry-specific products and policy at the Board of Directors and Executive Management levels to not only meet the needs of prospective clients, but to further establish a competitive advantage; distancing CNOB from other financial institutions by way of understanding the nature of the independent school business model and cash flow cycle of these unique, mission-based organizations. Beginning with the FSVP, Team Lead to all Loan Officer(s), Portfolio Manager(s) and Credit Analyst(s), the expectation is that this market expertise will continually strengthen, further developing trust both internally and externally within the school industry. While the nature of this trust can be seen by the timely direct access and support that the ISDB receives from key decision makers i.e., Executive Management, it should also be demonstrated by creating and maintaining a culture of personal empowerment where team members' feel confident in acting with a sense of urgency to make sound decisions regarding client relations and credit or portfolio management. The proposed organizational enhancement entails a continued investment in the personal development of specialized team members and talent familiar with the industry to continuously source quality business while maintaining a sharp focus on the overall quality of the portfolio versus the "ins and outs" of each individual opportunity presented to the Division. This will work to further cement CNOB's place as an industry leader in serving independent schools.

In developing specialized products and services to meet the needs of independent schools, it has been determined that the ISBD's intentions and efforts should remain focused on establishing an industry-wide reputation as a team of subject matter experts. The ISBD will possess the knowledge, resources, and capabilities to act in an advisory capacity to potential clients, provide schools with an extensive range of choices in banking products and services that have been developed with their unique needs in mind. From extending significantly large bond/credit facilities to schools for the completion of extensive capital projects to managing operating daily cash needs i.e., the collection and disbursement of funds in a secure, automated fashion, the ISBD will offer valuable and appropriate insight and guidance as to the most effective methods to manage their financial resources. ISBD team members must employ a proactive approach to assessing and understanding the banking needs of existing and prospective school clients to drive investments in system enhancements to strengthen the Bank's ability to expand its reach and increase its competitive advantage in various markets along the Eastern Seaboard, despite the absence of CNOB brick and mortar locations outside of the New York Metropolitan Area.

With a noted physical presence in New Jersey, New York, and South Florida, this initiative will consider the "where" and "why," including how far out of the Bank's current physical footprint the ISBD should dedicate its resources and efforts in order to garner attractive client relationships. To better understand and determine which schools and/or markets are attractive to the Bank, the ISBD team will dedicate time and financial resources to travel to attend various industry association conferences/meetings deemed valuable and beneficial to further develop relationships with existing and prospective clients and gain insight into industry trends**.** This exposure will help the ISBD better understand not only the large-scale economic challenges facing these schools, but also gain exposure to the offerings of other financial institutions who are active in this market, with who CNOB competes, and the way in which they respond and evolve to meet the changing needs of independent schools.

Business Development Efforts and Referral Sources

CNOB currently maintains relationships with leaders within the independent school industry along the East Coast. These relationships include Investment Bankers, Bond Counsel Legal Firms, Accounting and Audit Firms, School Associations, and their Heads/Executive Directors, along with other industry-specific professionals. Through these relationships, most often investment banking firms, the Bank's ISBD receives requests for banking proposals for various independent schools seeking financing for the needs discussed above. In further pursuit of new client acquisition, certain members of the ISBD will travel to attend various industry association conferences and annual meetings along the East Coast to network with potential clientele to demonstrate through conversation and/or presentations to independent school business officers and members of Boards of Trustees the value proposition of banking with CNOB. Additional business development efforts of the ISBD include the following:

- Further development of methods to garner business and serve schools from a value-based, advisory capacity rather than a cold sales approach such as being "the cheapest shop in town for loans and the highest rates on deposits."
- Identifying and joining professional school industry associations at the national, state, and local levels which may lack the presence and support of banking partners. Imperative to these efforts is remaining consistent in attending association events to further expand brand awareness by way of adding true value.

Institutional Competition

Building a team who understands the unique financial needs and cash flow cycle of the independent school model and is subsequently able to tailor bank products and services to complement that cycle requires commitment from an organizational perspective. While many traditional and/or larger commercial or money center banking institutions frequently fail to dedicate the appropriate resources to understanding the financial requirements of these schools', the ISBD will work to provide them with individualized solutions. That said, CNOB is not the only financial institution to recognize the potential of banking these schools. Top competitors in this space, many of which do in fact have dedicated independent school banking teams, consist of banks such as First Republic Bank, PNC Bank, Chase Bank and Truist Bank to name a few. While these institutions may be notably larger than CNOB from a balance sheet perspective, the ISBD's competitive advantage will remain its ability to understand the needs of these schools and dedicate significant human and financial resources solely to developing and growing this vertical within the Bank.

Credit Underwriting Standards and Considerations

When examining the functions of credit and lending at any financial institution, it is important to understand what exactly the Bank is lending money to finance, and most importantly, how will the Borrower generate the cash to repay the loan's principal balance plus interest. As such, CNOB credit approvals are based on the expectation of repayment in full by borrowers according to the terms and conditions as included in the applicable loan documents. In the school vertical, approval terms are based on the financial review and analysis of the historical, current, and forecasted cash flows generated by the borrower through operations, annual giving, and capital campaign pledge receipts, compared to their total current and proposed annual debt service. Additional considerations may be balance sheet metrics including total assets, total liquidity, total debt to net assets and total liquidity to total debt. The borrower's historical student enrollment trends and forecasted enrollment figures will be strongly considered when assessing the adequacy of cash flows relative to total annual debt service. While independent schools will most certainly experience fluctuations in student enrollment based on various factors, a thorough review must be conducted to assess sustainability.

As independent schools often utilize unique and complicated credit structures when compared to typical for-profit businesses or real estate entities, it is imperative that ISBD team members understand the types of credit products that schools seek and the how to price these facilities competitively to both win the business and generate substantial revenue for the Bank. The borrowings of independent schools are most often classified as Commercial and Industrial (C&I) loans as opposed to Commercial Real Estate (CRE) loans. A School's cash flow relative to the level of annual debt service is the key credit consideration in this market vertical. CNOB's value proposition here is the knowledge and experience to structure these borrowings (often the issuance of sizeable tax-exempt bonds) in a manner that is mutually beneficial to the School and the Bank. The following CNOB credit products are unique to independent schools:

- **<u>Direct Purchase Qualified 501(c)(3) Bonds</u>:** (Tax-exempt and taxable, draw-down and single-advance bonds) issued by governmental authorities.
- **<u>Terms Loans to Finance</u>:** Capital improvements, construction, real estate acquisition, refinance term debt, equipment purchases, costs of bond issuance
- **<u>Capital Campaign Bridge Lines of Credit</u>:** Advances on the line of credit used to bridge capital campaign pledge receipts for the funding of capital projects and construction.
- **<u>Working Capital Lines of Credit</u>**: Bridge potential working capital shortfalls.
- **<u>Letters of Credit</u>:** Used to support construction projects or lease commitments.

Note: As most independent schools are organized as nonprofit or not-for-profit 501(c)(3) corporations, personal and/or corporate guarantees do not apply to the borrowing structure of these credit facilities. They are therefore considered non-recourse loan facilities.

Loan Pricing and Portfolio Management

The pricing of loan facilities considers the credit risk/profile of the borrower, loan size, type of facility, term, fixed rate interest period and overlying market conditions. As is unique to the ISBD (and non-profit lending in general), pricing of certain specialized structures such as tax-exempt bonds must consider the tax equivalent yield to the Bank when determining the proposed pricing of credit facilities. After the extension of credit to various independent schools, The ISBD will be responsible for tracking the receipt of financial reporting, completion of annual reviews indicating loan covenant compliance, and the timely receipt of all payments due with consideration to interest rate resets and credit facility term-outs. As discussed above, the Division will include designated positions which define the responsibilities of all Team Members.

Implementation Timeline

Led by the Project Leader in direct collaboration with the FSVP, Business Development Team Leader, the proposed build out of the ISBD should be completed within a timeframe of twelve (12) months. With emphasis placed on achieving high-quality end results as it relates to human resources management, product and service development, policy and procedure and accountability measures, this schedule is subject to change:

I. Obtain buy-in and support from Executive Management; upon subsequent approval, develop budget and timeline for essential human resource growth/management and financial investments in the ISBD's business development efforts.

II. Recruit and hire new personnel with dedicated roles and responsibilities within the ISBD. Utilizing CNOB talent and human resources team outreach via numerous avenues such as website postings and contracting top recruiting firms to find and place qualified and experienced candidates. This will allow for a faster scaling of the Division.

III. Design and present a suite of specialized products and services, both credit and non-credit, tailored to the needs of independent schools. This will include collaboration and buy-in from CNOB Credit Officers, Executive Management Team and the Board of Directors as certain proposed products may pose exceptions to current credit/loan policy.

IV. Invest in the professional development and educational advancement of team members and develop a formal employee training program. In addition to company-wide onboarding process, new hires will need to complete training to include non-profit accounting and credit underwriting. New team members are expected to gain knowledge of all technology platforms and Bank systems to become self-sufficient. Training will include use of [redacted] loan origination platform [redacted] to be provided by the Bank and various organizations such as the American Bankers Association.

V. Identify ongoing opportunities for business development: Focus efforts on targeting schools through various sources including but not limited to purchasing memberships and sponsorships to various Independent School (Accrediting) Associations, deepening relationships with Financial Advisory firms who represent certain schools in debt structuring transactions, and attending industry events to gain knowledge of market trends. Establish reliable and productive working partnerships with a variety of educational institutions. It will be vital for the ISBD to establish solid working ties with educational institutions if they wish to attract the patronage of those institutions and secure the business they offer.

VI. Plan and hold monthly meetings with all team members and internal partners such as Cash Management Team or Retail Teams to discuss pipeline management and the state of affairs within the Division. These meetings should include discussions around both successes and failures; as well as challenges and recommendations of ISBD team members.

Assumptions for Implementation

Successful implementation of the Independent School Banking Division will require that certain assumptions such as buy-in from Executive Management to create a specialized team and continued mission alignment of ISBD team members are carried out. If these assumptions transform into action, both the ISBD and CNOB overall will continue to experience growth and profitability. Below are milestones which should be included in the ISBD rollout blueprints:

I. Formalize the ISBD by way of dedicating team members and human resources to the work and goals of the Division.

II. Product and service development and implementation which includes revising and updating Bank credit policy to tailor loan products to meet the borrowing needs of independent school clientele.

III. Organize and maintain loan portfolio; establish metrics and functions for management and maintenance of credit facilities i.e., maturities, renewals, extensions, and covenant compliance.

Part III: Financial Impact

Investment and Expense Requirements

The proposed initiative of formalizing the CNOB Independent School Banking Division is a sizeable investment for the Bank both in terms of dollars and human capital with successful implementation requiring ongoing input and collaboration from various areas of the Bank. Most notably, high level buy-in from Executive Management and the Board of Directors, the Bank's Credit and Risk Management Teams, as well as the Bank's Cash Management and Retail Banking Teams. Cost estimates in dollars associated with the proposed ISBD initiative include the following assumptions:

- **Salaries and Benefits of Team Members**: As included in the organizational chart on Page 19, the Division should initially be staffed by six full-time Bank employees. These employees will serve as subject matter experts within the ISBD. The result of which will create greater operational efficiency within the Bank in the form of reduced friction for clients seeking solutions and the response time in which clients' requests are fulfilled. This improved client experience will lead to increased market share for both the ISBD and CNOB. The total annual compensation for the Division is expected to be approximately $775M and is broken down as follows:

Team Member Role	Annual Compensation	
FSVP/Division Team Lead	$	250,000
VP/Loan Officer	$	160,000
AVP/Portfolio Manager	$	140,000
Cash Management Assistant	$	75,000
Credit Analyst II	$	80,000
Credit Analyst I	$	70,000
Total Annual Compensation	**$**	**775,000**

- **Investment in Business Development Efforts**: Financial support and sponsorship of client fundraising efforts by way of annual giving/donations (since these 501(c)(3) entities are heavily reliant non-tuition revenue sources), attending and presenting at various industry conferences and annual independent school association meetings. The cost of these efforts is broken down as follows:

Business Development Effort Expenses	Annual Membership Cost	
Membership Cost of CAIS *(Connecticut Association of Independent Schools)*	$	4,000
Membership Cost of NYAIS *(New York Association of Independent Schools)*	$	4,000
Membership Cost of VAIS *(Virginia Association of Independent Schools)*	$	3,000
Membership Cost of NJAIS *(New Jersey Association of Independent Schools)*	$	4,000
Membership Cost of AISGW *(Association of Independent Schools of Greater Washington)*	$	3,000
Membership Cost of FCIS *(Florida Council of Independent Schools)*	$	4,000
Membership Cost of NBOA *(National Business Officers Association)*	$	8,000
Total Annual Association Membership Cost	**$**	**30,000**

- **Annual Giving**: In addition to the above stated costs, which are directly tied to the Bank's involvement with state and regional associations, CNOB also provides additional support by way of annual giving to member Schools who are clients. Giving to these organizations typically totals $5M per school on an annual basis and is expected to be as follows:

Annual Giving	Total Cost
Annual Giving = $5,000 per School (Estimated Total of 15)	$ 75,000

- **Travel and Entertainment**: Given the scope of the new ISBD within the Bank, travel will be required for client facing individuals. Travel will be primarily comprised of airfare and mileage up and down the Eastern Seaboard, with lodging and meals included. The Bank typically holds a formal dinner reception for invites from each association noted on the prior page. With that, estimated travel and entertainment expense of the Division is expected to be as follows:

Travel and Entertainment Categories	Annual Cost
Annual Travel (Mileage and Airfare)	$ 10,000
Hotel Stays	$ 6,000
Dinner and Receptions	$ 24,000
Total Annual Cost	**$ 40,000**

Note: Certain items which are not considered above consist of location and rent expense. This was not included as the proposed ISBD team members will occupy space within existing branch offices which is not currently occupied. No significant outfitting or equipment expenses will be required as the Bank has space that is ready for use.

Interest Expense

The infrastructure expense of the ISBD vertical within CNOB is anticipated to total approximately $900M for the first year ending 12/31/2023. Please note that the true capital outlay necessary to both attract and hire additional talent to build out the Division is subject to change based on factors such as experience and production. While infrastructure expenses are expected to total just over $900M, the projected interest expense on deposits is more challenging to determine due to the volatility of the current rising interest rate environment. For this Capstone Initiative analysis, it is assumed that the Division's deposit portfolio at fiscal year-end 12/31/2023 totals $45,000M.

Revenue Generation

Revenue generation will be derived from interest earned and fee income on the ISDB's loan portfolio. While independent school clients and their respective Boards of Trustees are certainly educated and capable when evaluating interest rate risk, the value associated with the CNOB client experience will serve as a competitive advantage in a market sector where other competitors may be able to offer lower loan pricing. With this approach in mind, the ISBD will be tasked with growing its loan portfolio year-over-year, along with associated deposit balances. Based upon that, the Project Leader forecasts a loan portfolio total of $145MM at fiscal year-end 12/31/2023. Included in this forecast is an estimated average yield of 5% on the loan portfolio (notably inclusive of tax-exempt bonds), which is subject to change as future interest rates fluctuate. As illustrated in the following income statement for fiscal year 12/31/2023, the ISDB's projected net income equals $3,908M. Looking forward over the next five years, the Division has determined that annual portfolio growth on a percentage basis beginning with 25% in years 2023-25, followed by 20% in years 2026-27. The following income statement includes these projections:

ISBD Projected Income Statement FY's 2023-2027

Revenue	**FY 2023**	**FY 2024**	**FY 2025**	**FY 2026**	**FY 2027**
Loan Interest Income	$ 7,250,000	$ 9,062,500	$ 11,328,125	$ 13,593,750	$ 16,312,500
Fee Income	$ 250,000	$ 312,500	$ 390,625	$ 488,281	$ 585,937
Total Revenue	**$ 7,500,000**	**$ 9,375,000**	**$11,718,750**	**$14,082,031**	**$16,898,437**
Expenses					
Personnel	$ 775,000	$ 813,750	$ 854,437	$ 897,158	$ 942,015
Operating and Overhead	$ 125,000	$ 125,000	$ 125,000	$ 125,000	$ 125,000
Marketing	$ 10,000	$ 12,000	$ 14,000	$ 16,000	$ 18,000
Travel and Entertainment	$ 40,000	$ 40,000	$ 40,000	$ 40,000	$ 40,000
Donations	$ 75,000	$ 85,000	$ 95,000	$ 105,000	$ 115,000
Interest	$ 900,000	$ 1,125,000	$ 1,406,250	$ 1,687,500	$ 2,025,000
Allowance for Loan Loss	$ 1,667,500	$ 2,084,375	$ 2,605,468	$ 3,126,561	$ 3,751,873
Total Expenses	**$ 3,592,500**	**$ 4,285,125**	**$ 5,140,155**	**$ 5,997,219**	**$ 7,016,888**
Net Income	**$ 3,907,500**	**$ 5,089,875**	**$ 6,578,595**	**$ 8,084,812**	**$ 9,881,549**

Assumptions for Projected Growth

Assuming total annual revenue growth desired by the ISBD is achieved, various expenses will also increase year-over-year in-line with projected revenue growth. The expenses included in the income statement above consider the following changes/increases:

- Personnel expense is expected to increase a minimum of 5% annually based on salary increases of existing team members and potential new hires.
- Operating and overhead expenses should remain flat at approximately $125M annually over the next five years as the Bank currently maintains both office space and resources for employee use.
- Marketing expense is projected to grow incrementally by $2M annually over the next five years as the portfolio and client base expands. The same should ring true for travel and entertainment as well as client giving/donations assuming the Division keeps pace with its growth goals.
- The interest expense is calculated as 2.5% of 80% of deposit balances totaling $45MM (interest-bearing). The remaining 20% of total deposits are assumed to be DDA funds.
- The allowance for loan loss expense is expected to increase in-line with asset growth and is calculated as 1.5% of the total estimated loan portfolio of $145MM (Per CNOB metrics).
- Based on these assumptions, the ISBD projects notable increases to net income over the next five years; growing from $3,908M in FY 2023 to $9,862M in FY 2025.

Financial Risks and Mitigants

Looking at the greater banking industry, notwithstanding the atypical growth in 2020 as a result of a COVID-19 fueled deposit surge, most institutions find it challenging to attract and retain core deposits from clients; specifically, non-interest-bearing balances which are ultimately utilized to fund loan growth. According to an article published by the Federal Reserve Bank of St. Louis entitled "Banks

Navigate Surging Deposits, Tepid Loan Activity Since COVID-19 Onset[11], *"Slightly more than one-third of surveyed bankers said the cost of funds was the factor most likely to influence future profitability, ahead of loan demand, operating costs, loan rates and regulatory costs. The availability of core deposits—generally defined as consumer savings accounts, consumer and business checking accounts, and money market funds—was seen as a persistent problem that would only be exacerbated by a proliferation of new entrants and technologies into the banking system."* As such, a significant challenge to the ISBD and the larger CNOB remains in the ability to offer existing and prospective school clients' competitive loan and deposit pricing to both retain and win new business in a competitive industry while simultaneously lowering the cost of funds and increasing profitability/net interest margin (NIM) for the benefit of the Bank and its Shareholders.

Notably, potential school clients targeted by the ISBD have remained resilient over many years because of the strong financial conditions existing within their institutions and the affluent nature of their larger communities. Most displaying strong liquidity (cash and investments) and low debt-to-net-worth, these schools are committed to preserving their respective missions. Further, the business won by the ISBD often includes long-term financing arrangements (up to 30-year loan term commitments) which contractually require clients to maintain their full and often sizeable deposit relationships with CNOB for the life of the credit facilities. These relationships are therefore very advantageous to the Bank, making the investment in the development of the ISBD well worth the associated costs over time.

This strategic initiative will allow the Bank to capitalize on the opportunity to service an arguably underserved niche market vertical with immense potential for long-term growth and development. This should further result in improved profitability and the strengthening of CNOB's financial position. Assuming the containment of current pricing within the existing loan portfolio, and the retention of

[11] https://www.stlouisfed.org/on-the-economy/2021/august/banks-navigate-surging-deposits-tepid-loan-activity

strong DDA deposit balances maintained by independent school clients, the Bank's cost of funds can be reduced, thereby increasing the net interest margin. While the current volatile interest rate environment can lead to increased profitability on the loan side, members of the Division must remain vigilant in their client outreach and deposit retention efforts.

Part IV: Non-Financial Impact

Importance of Company Mission and Culture Alignment

While growing pains are most always a constant when introducing/implementing a new line of business, the responsibility of obtaining and retaining employee buy-in remains with the Founder(s) and Management Teams within an organization. Serving as the ultimate authority, Management is charged with the task of continuously evolving in order to keep pace with ever-growing client expectations.

ConnectOne Bank was founded on the guiding principle of putting *"People First."* Vying for market share in one of the most saturated and competitive geographical areas in the world i.e., the New York Metropolitan Area, the Bank has realized rapid growth (approaching $10B in total assets) as a result of employing a clearly established mission and set of core values which are utilized by team members when making decisions. Employee engagement, including feeling empowered to make sound choices to delight clients, must remain paramount. In her article entitled, *"Making the Business Case for Organizational Guiding Principles*[12]*,"* Organizational Strategist Nicki Gibbs succinctly describes the importance of this alignment as she states, *"Organizations that align employee behavior and decision-making with guiding principles will achieve better business results. Organizational guiding principles, which may also be known as company values, company principles or company beliefs, summarize what*

[12] Gibbs, N. (2020, Mar 27), Making the Business Case for Organizational Guiding Principles.

an organization believes and the behaviors it agrees to live by every day. They promote thinking and actions that are both authentic to the organization and also align with its future goals.[13] *"*

Much like a multi-billion dollar, publicly traded financial institution such as CNOB, independent schools utilize values-based decision-making models in their approach to operations and student education. These cultural similarities across institutions seem more important now than ever before. As prospective clients spanning various geographic areas often choose their business partners/vendors based on mission and value alignment, the ISBD must consistently provide a high level of service to realize sustained growth. To further quote Nicki Gibbs, *"The business impact of guiding principles goes beyond internal metrics. Consumers are also choosing which brands to purchase from based on whether the company reflects their values.* ***A recent survey from Accenture***[14] *found that sixty-three percent of consumers "prefer to buy goods and services from companies that stand for a shared purpose that reflects their personal values and beliefs and are ditching those that don't. Consumers are more likely to bring business to companies that stand for something."*

Potential Organizational Hurdles

- **Buy-in from Executive Management and Board of Directors**: With most of the independent schools targeted/banked by the Division being mission-based, non-profit entities with 501(c)(3) status under the IRS tax code, they have the option to borrow funds utilizing unique vehicles such as tax-exempt bond issuances. As this financing structure involves the Bank extending often sizeable, long-term commitments to schools without the security of personal or corporate guarantees, these loans are non-recourse facilities. With that in mind, it will be important for members of the Division

[13] https://beehivepr.biz/business-case-guiding-principles/

[14] https://www.businesswire.com/news/home/20181205005061/en/Majority-Consumers-Buying-Companies-Stand-Issues-Care

to thoroughly understand and manage the credit risk and pricing of these financings to mirror the risk appetite of Executive Management and the Board of Directors, and successfully garner approval to move forward. Understanding that tax-exempt bond facilities will negatively affect the Bank's NIM as the gross, tax-exempt interest rates will be lower than the taxable equivalent rates offered by other lending areas of the Bank, the ISBD must communicate the value in winning the full client relationship, focusing largely on the above average relationships, to grow and maintain a healthy overall portfolio.

- **Attracting and Maintaining Quality Talent:** As is the case with other specialized lines of business, the growth of the ISBD portfolio is highly dependent on possessing a robust team of subject matter experts who can provide high quality, timely client support. Along with new client acquisitions, the Division must grow in-kind to warrant sufficient resources to perform all required functions, including management of the loan portfolio, structuring and maintenance of deposit accounts and the implementation and ongoing support related to treasury services utilized by clients. Understanding that any specialized areas come with a high learning curve, new team members must have the capability to learn the "ins and outs" of the market vertical quickly. As future growth is ultimately realized, it will be imperative that the Bank dedicate adequate human capital and financial resources to the Division.
- **Establishing and Maintaining Positive Interdepartmental Relations**: The addition of a new Division may create friction between various teams or departments within the Bank; specifically, with regards to overlap in the business development efforts of various Bank Officers. The ISBD must establish and maintain a positive reputation and work in a collaborative fashion with other departments and officers of the Bank, who are also working to meet established goals, to win new business and support existing clients. By holding department-specific meetings and informational

training sessions, the ISBD will formally introduce the market vertical and educate other departments about the work of the Division to create complementary and mutually beneficially working relationships with other areas of the Bank. Communication and transparency will be key in achieving this goal.

Potential External Challenges

- **Effectively Communicating the Value Proposition:** Seemingly operating more like a technology start-up firm than a traditional commercial bank, CNOB employs an efficient, branch-lite operating model which places more focus on the quality of the Bank's product and service offerings than its physical branch presence. As such, ISBD team members must be able to effectively convey the greater value of establishing a full banking relationship with CNOB. In a competitive landscape where client borrowings are often inclusive of sizeable, long-term credit facilities, Team Members must be able to successfully communicate the qualitative and quantitative benefits beyond loan interest rates. While certainly striving to be aggressive with pricing, CNOB does not utilize a "cheapest shop in town" approach nor does the ISBD feel compelled to bid on every opportunity it comes across. Acting as subject matter experts, ISBD team members will be proficient in speaking to all CNOB products and services that prospective schools and their Business Officer's will have at their disposal. Placing a significant emphasis on investments in new deposit and treasury management solutions, CNOB's offerings are just as robust, if not more so than other banking institutions.
- **Managing Industry Reputational Risk:** As the continued alignment of mission and action should serve as a competitive advantage for the ISBD in its business development efforts, deviation from this philosophy by team members can be detrimental to the reputation of the Division and the Bank

at-large. Like other industries, the Business Officers of independent schools often communicate with one another via online professional platforms, as well as in-person at industry association conferences or meetings. To put it simply, if a CNOB school client is unhappy with a product or the level of service they receive, the chances that other clients or prospects will hear about that experience are high. This reputational risk must be considered and managed appropriately by members of the ISBD, from the top down. Ensuring that communication and education around organizational enhancements are ongoing is imperative to the growth and success of the Division. While perhaps not always considered a top priority in the past, the importance of the client experience has grown exponentially in recent years to become a substantial determinant in choosing a banking partner. Making decisions based on the Bank's guiding principles, which includes keeping the CNOB Mission and Core Values *(Appendix A: ConnectOne Bank's Mission and Core Values)* top of mind, will lead to greater success in measurable metrics including new client acquisition, increased profitability, and continued expansion of the Bank's balance sheet. As ISBD team members are challenged to approach their job functions in a manner that works to *"Make an Impact"* on the individuals and greater communities they serve, the Division will ultimately provide mission-based banking solutions and support to its mission-based independent school clients. In partnering with and advising these schools on how to successfully manage their financial resources and structure their debt/borrowings to improve and expand their institutions, the ISBD will help further cement CNOB's position as a leader in the independent school banking space. It is the Project Leader's opinion that when team members successfully carry out the Bank's mission, clients will be better positioned to realize their own missions of educating and developing their students and communities.

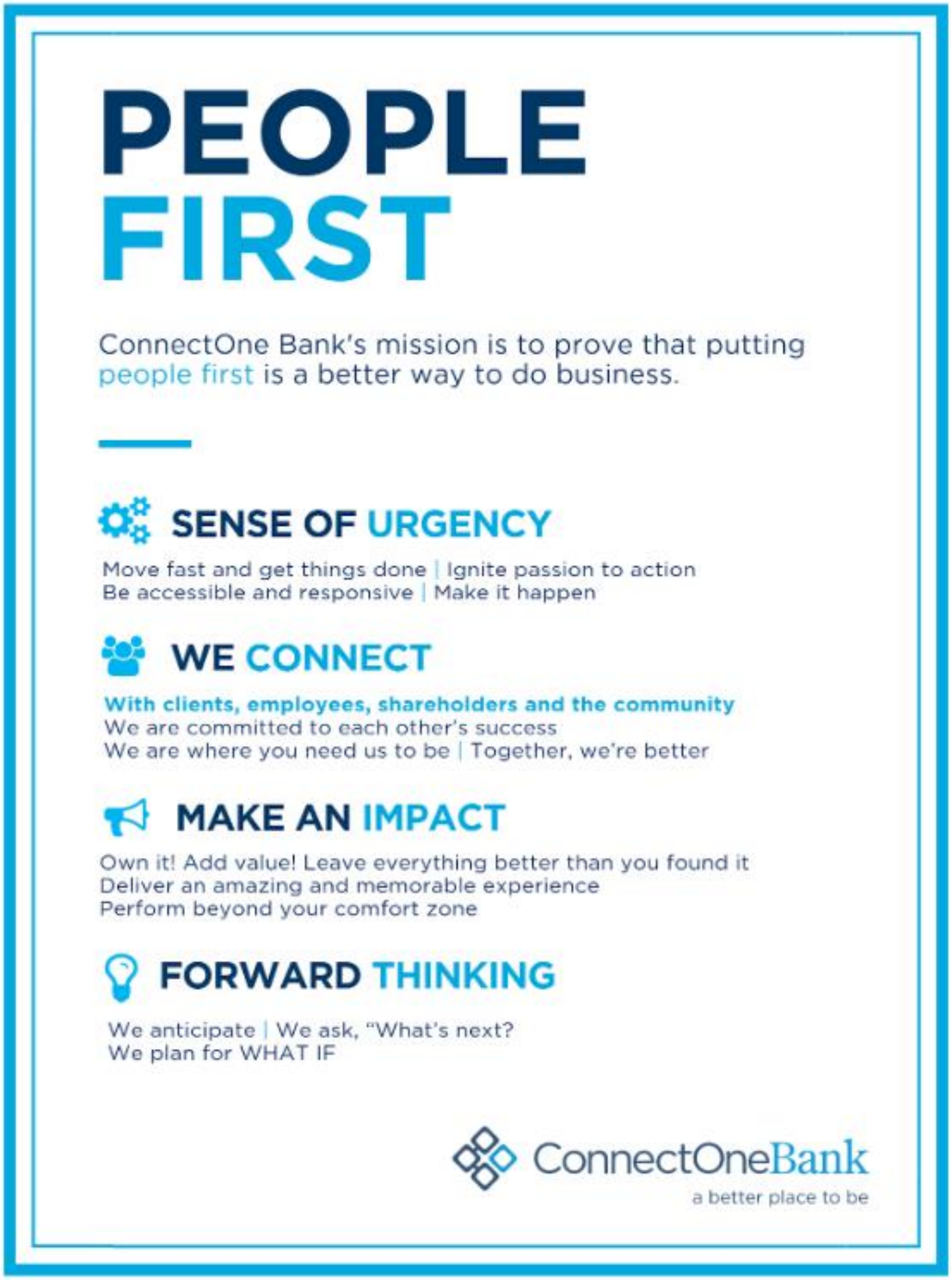
Conclusion

As a mission driven, forward-looking financial institution with a lean brick-and mortar presence, ConnectOne Bank may seem to have more in common with a Silicon Valley-based financial technology start-up firm than a traditional commercial bank. The result of a strong culture that encourages personal and professional development and empowerment, team members in all areas of the organization are invited to step out of their comfort zone in order to challenge the status quo and continuously further their knowledge and skillset. Seizing opportunity is an action embedded in the culture of CNOB. As the Bank continues to experience rapid growth, team members must remain nimble and focused on what drives both clients and prospects in making financial decisions for themselves or their business. Identifying client needs and working to exceed expectations is at the core of ConnectOne Bank's mission of "People First."

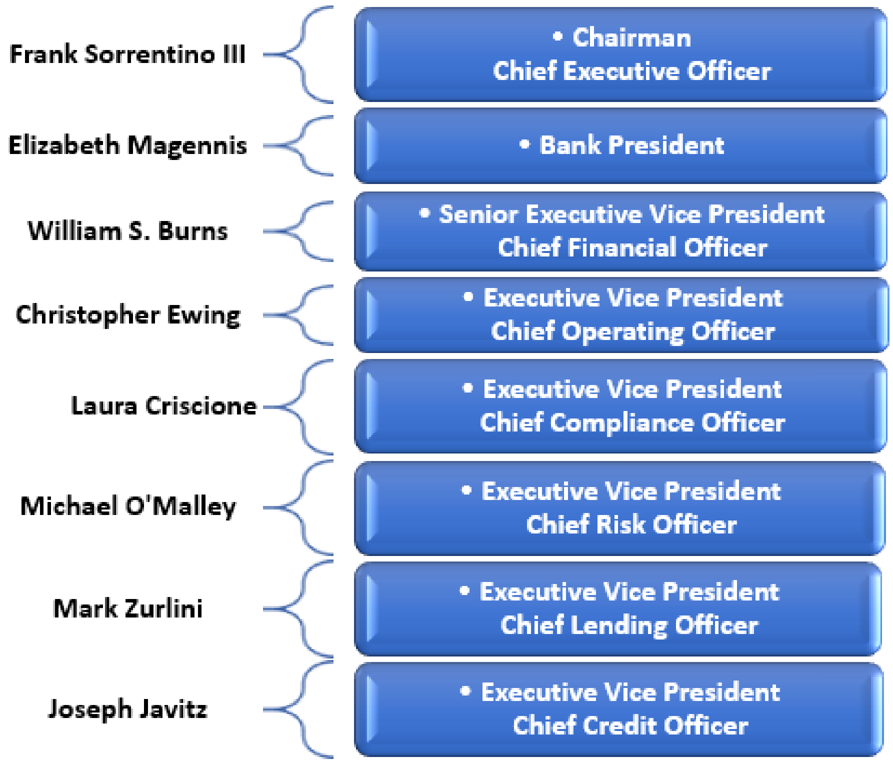
The proposed subject strategic initiative above is designed with this very mission in mind. Recognizing opportunity and making bold decisions to benefit both clients and the Bank are the reasons that CNOB is the unique institution it is today. While scaling the Independent School Banking Division will require significant investments of both financial and human resources, as well as close risk management, the potential for growth and profitability is boundless. From a credit perspective, establishing a sizable, high-quality loan portfolio will generate significant revenue for the Bank and should be looked upon favorably by Management. Furthermore, the deposit relationships gained as a result of these borrowings will work to reduce the Bank's overall cost of funds, creating additional value. In consistently operating with the Bank's core values at the forefront, the Independent School Banking Division can establish an industry reputation of being the premier banking partner for Independent Schools along the Eastern Seaboard. With the buy-in and support of Executive Management and the Board of Directors, the Division will function using the very same mission and principals by which

CNOB operates day in and day out, from the top of the organization down. Earning the trust of clients by consistently exceeding expectations is what truly makes ConnectOne Bank “a better place to be.” As such, the Project Leader is recommending that Management approve the proposed strategic initiative as outlined herein and move forward with the establishment of the Independent School Banking Division.

<u>Appendix A</u>: ConnectOne Bank’s Mission and Core Values



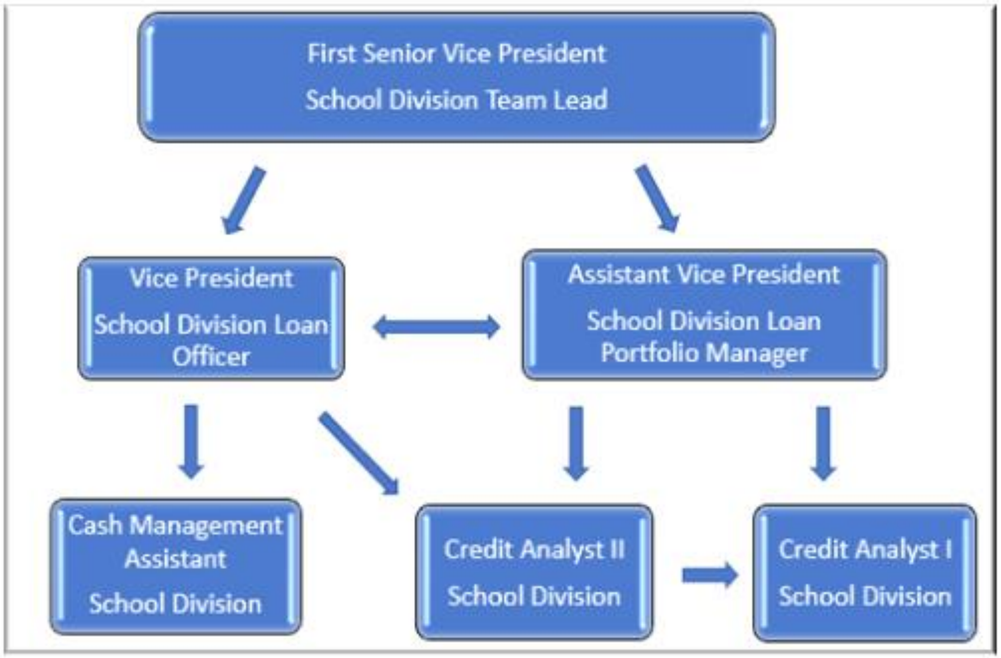
Appendix B: Executive Management Team Hierarchy



Appendix C: FDIC-Insured Institutions Deposit Market Share Report (as of June 30, 2022)

Selected Market					June 30, 2022				
State: NEW JERSEY	County: ALL	City: ALL	Zip Code: ALL		Outside of Market		Inside of Market		
Institution Name	CERT	State (Hqtrd)	Bank Class	State/ Federal Charter	No. of Offices	Deposits ($000)	No. of Offices	Deposits ($000)	Market Share
Bank of America, National Association	3510	NC	N	Federal	3,700	1,884,390,143	205	79,650,717	17.20%
TD Bank, National Association	18409	DE	N	Federal	936	294,138,690	226	62,219,625	13.43%
Wells Fargo Bank, National Association	3511	SD	N	Federal	4,528	1,393,177,943	238	48,856,057	10.55%
PNC Bank, National Association	6384	DE	N	Federal	2,388	401,533,076	227	45,147,971	9.75%
Jpmorgan Chase Bank, National Association	628	OH	N	Federal	4,626	2,086,426,962	192	42,035,038	9.08%
Valley National Bank	9396	NJ	N	Federal	110	22,254,390	130	21,661,955	4.68%
Citizens Bank, National Association	57957	RI	N	Federal	1,048	166,815,588	119	14,750,780	3.18%
Santander Bank, N.A.	29950	DE	N	Federal	377	58,632,856	105	13,239,281	2.86%
Provident Bank	12010	NJ	SB	State	7	547,467	92	10,371,343	2.24%
Oceanfirst Bank, National Association	28359	NJ	N	Federal	6	701,033	36	9,208,689	1.99%
Lakeland Bank	19953	NJ	NM	State	1	174,005	68	8,369,346	1.81%
Columbia Bank	28834	NJ	SB	Federal	0	0	66	7,893,829	1.70%
Capital One, National Association	4297	VA	N	Federal	275	307,507,429	21	6,448,120	1.39%
Manufacturers and Traders Trust Company	588	NY	SM	State	1,011	167,062,359	65	6,014,003	1.30%
Connectone Bank	57919	NJ	NM	State	8	859,675	15	5,873,252	1.27%
Kearny Bank	28765	NJ	SB	State	3	101,406	43	5,854,601	1.26%
Peapack-Gladstone Bank	11035	NJ	SM	State	0	0	21	5,417,217	1.17%
Fulton Bank, National Association	7551	PA	N	Federal	151	16,588,879	57	4,653,805	1.00%
Cross River Bank	58410	NJ	NM	State	1	85,652	1	4,541,441	0.98%
Sumitomo Mitsui Trust Bank (U.s.a.) Limited	27054	NJ	NM	State	0	0	1	3,172,707	0.68%
Spencer Savings Bank, SLA	30076	NJ	SL	State	0	0	27	3,139,078	0.68%
Citibank, National Association	7213	SD	N	Federal	667	760,213,000	9	3,093,000	0.67%
New York Community Bank	16022	NY	SB	State	196	38,343,900	41	3,032,883	0.65%
Republic Bank	27332	PA	NM	State	17	2,200,106	19	3,014,052	0.65%
Truist Bank	9846	NC	NM	State	2,095	432,533,028	23	2,909,972	0.63%

<u>Appendix D</u>: Proposed Independent School Banking Division Hierarchy



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Date of Report (Date of earliest event reported): September 7, 2022
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