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ERF banks on growth in financial services arena

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On the morning after Hurricane Rita made landfall in September 2005, Jim Fazende woke up to a communications nightmare.

Rita's storm surge and winds knocked out power to the head office of First Federal Bank of Louisiana and several of its 13 branches for about two weeks, affecting some 20,000 customers. Branches further north had to operate without computers.

Fazende, First Federal chief operating officer, recalls it as a challenge he prefers not to face again. As a result, First Federal has just inked a \$1 million deal with League City-based ERF Wireless Inc., which is banking on a breakthrough in several storm-affected markets across the southern United States with its BranchNet and BankNet wireless broadband communications networks aimed at the financial services market.

The fact that a First Federal competitor that had previously signed up with ERF was still up-and-running right across the street from one of Fazende's branches in Lake Charles during the storm was certainly an eye-opener.

Says Fazende, "We feel that with this system we can be up and running much quicker after a disaster."

John Burns, CEO of ERF's enterprise network services division, says this contract represents the cutting edge of the company's long-term strategic plan. ERF is in talks with other potential banking and credit union customers in the state, part of a target to line up 19 more financial institutions by 2012.

According to Fazende, the main reason the bank decided to go with ERF's technology had more to do with concerns about bandwidth than worries about bad winds.



MICHAEL STRAVATO/HBJ

H. Dean Cubley of ERF Wireless: 'It takes time to develop credibility in the banking industry, and you have to do it on a bank-by-bank basis.'

With high-speed data, high-definition video conferencing and remote video training becoming more important to his business, Fazende faced some heavy infrastructure costs if he wanted to bring those services to his branches using leased telephone company trunk lines.

"It was pretty cost-prohibitive for us to try to connect all of the branches, and ERF could provide 10 times the bandwidth for pretty much the same as we are paying now," Fazende says.

Still, in order to pass muster from banking regulators, the system had to have substantial encryption software, considering it involves transmitting customers' sensitive financial and personal data. ERF's BankNet carries a triple-encrypted security firewall known as CryptoVue.

"You've seen the headlines about financial institutions losing personal data," says

H. Dean Cubley, ERF chairman and CEO. "Banking regulators are most concerned about the possibility of a bank employee routing customers' data outside to a third party, so we came up with the security mechanism to prevent that."

Use of the network system at the bank includes a special key — like those used to launch military missiles — that only the bank manager possesses, plus the encrypted software barriers.

TWO FOR THE ROAD

Cubley says although the BankNet system may represent a long-term growth opportunity for corporate customers with a cash-generating upside, publicly traded ERF is making much faster inroads these days in one of its two other product areas that have bigger up-front payoffs.

The company expects to complete instal-

ERF: Wireless firm hopes niche product takes financial services sector by storm

lation in September of a \$2 million fiber-optic private voice, video and data network for a luxury gated community, El Dorado Golf and Beach Club, comprised of multi-million-dollar homes in San Jose del Cabo, Mexico. Scottsdale, Ariz.-based Discovery Land Co. is the developer.

A third part of the operation is wireless networks for commercial and residential customers that compete with cable and telephone company products in several medium-size Texas markets, such as Lubbock. ERF currently serves 2,400 customers.

Though a predecessor company was incorporated in 1986, ERF did not become operational in its current form until 2004 with a name change and reverse stock split, when the shares began trading over the counter.

Cubley previously held several executive officer positions as a co-founder of direct access digital entertainment provider Eagle Broadband Inc., also of League City. He resigned his executive position in 2004 when he became a director and chairman of ERF, and cut formal ties to Eagle Broadband when he took the CEO job at ERF in 2006.

Majority control of ERF rests with family matriarch Frances Cubley through several trusts. The trusts, high-wealth individuals and institutional investors have pumped \$8 million financing into ERF so far.

The company has rolled up accumulative losses of about \$13 million, according to Securities and Exchange Commission filings. For the three-month period ended March 31, ERF had a net loss of \$1.3 million, or 5 cents a share, on revenue of \$505,000, compared to a net loss of \$715,000, or 8 cents a share, on revenue of \$862,000 a year earlier.

ERF shares closed at 36 cents on July 2, compared to a low of 9 cents earlier this year. Shares reached an all-time high of about \$11 in 2005. About 31 million shares are outstanding.

In June, to fund ongoing operations and expansion plans, ERF secured a private equity line of credit with Dutchess Capital Management LLC, which gives Dutchess the right to purchase as much as \$10 million worth of ERF shares at a seven percent discount to the market. As ERF draws on

the line of credit, Dutchess is awarded an equivalent number of shares.

Dutchess, with offices in Boston and LaGrangeville, N.Y., has a similar \$5 million line of credit set up with Cubley's prior firm, Eagle Broadband.

Still, with revenue projections of at least \$5 million for 2007 compared to \$1.7 million in 2006 — about 60 percent of revenue

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Jim Fazende
First Federal Bank of Louisiana

coming from the high-end residential community networks — the quest for the 46-employee ERF to reach profitability is at hand.

And with a regional bank on board with the statewide BankNet system, a long-term segment of the ERF business plan is finally in focus.

Says Cubley, "We've been in planning for three years to get up to this point, and now we're ready to roll out some contracts. It takes time to develop credibility in the banking industry, and you have to do it on a bank-by-bank basis."

FORMER AUSTIN TECHNOLOGY EXEC LEADS ERF INTO BANKING ARENA

The high-tech entrepreneur behind ERF Wireless Inc.'s foray into the banking world is John Burns, who brought the technology over in 2005 when the company acquired his latest enterprise, Skyvue USA



Burns

East Central Texas Inc.

Burns was also the founder of Austin-based online banking and bill paying services pioneer FundsXpress Financial Network Inc., ultimately selling the company for \$134 million in March to First Data Corp. of Omaha, Neb.

The BranchNet/BankNet system, aimed at banks in underserved or rural markets — particularly along the hurricane-prone Gulf Coast — can bundle data in speeds as high as 20 megabits per second, compared to traditional leased telephone company lines in those rural markets that typically handle only as much as 1.5 Mb.

A typical system installed at a bank branch includes a small \$50,000 transmission tower and Motorola Inc. hardware, as well as monthly fees of about \$750.

Paving the way for ERF's foray into the Louisiana market was a creatively crafted deal in which ERF is able to use space on the state's transmission towers set-up for the emergency communications, traffic video surveillance and 9-1-1 system, in exchange for providing a secure backup emergency system that can function in extreme conditions.

Four other small banks in three states are already BranchNet customers — including Cameron State Bank in Texas — but First Federal Bank of Louisiana is the first to connect to the initial section of the statewide BankNet system.

Burns says negotiations are already under way with officials in Texas, Mississippi, Alabama, Florida and Georgia to duplicate the Louisiana system tower infrastructure deal as a springboard into those markets for BankNet.

Jim Fazende, First Federal chief operating officer, says such a shared system, which helps keep costs down, should be attractive to other banks and financial services players that operate in rural areas and smaller cities that do not have upgraded telecommunications infrastructure.

"That use of the state's police towers (for the ERF system) is a real good idea," Fazende says. "That's a good concept we're buying into."

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