DO YOU NEED AN INTERNET ONLY BANK?

by Steve Brown

At strategic offsites, the current buzz is over starting an internet bank. With the success of Citibank direct, Zions, HSBC and ING Direct, banks have taken notice the ease at which some of these banks have gathered billions of deposits. ING Direct, started in 2000, now has $40B in savings balances, sells mortgages and will start offering checking next quarter. Citibank direct launched 6-months ago and now has $7B in deposits and offers home equity loans. A common misconception is that internet-only banks are about technology. It is not, as the same strategy can be accomplished in other brick and mortar ways (and it has). The beauty of the internet is that it is highly scalable and works well when marketing on rate. These internet-only banks really demonstrate the importance of channeling, a subject that we will be discussing in detail at our next High Performance Bank Workshop next week. Internet-only banking is more about segmenting your customer by rate sensitivity and convenience than anything else. Is it time for your bank to get involved? The answer is Â– probably not, at least not right now. For starters, an internet-only bank requires a cultural change. This is difficult for independent banks as it is their very nature to lavish service on the client. The bank must be ready to divert their customers to the web in order to contain costs since you are already paying a high rate. "You need account documents Mr. Customer? Please log onto www.myebank.com." "You want to know what the $25 dollars in fees are for? Please log in." If you are not ready to re-direct customers, then it will be a money losing proposition, as margins at internet banks are already razor thin. The bank must be prepared to create a separate brand and to service their customers electronically. In addition, the bank must be prepared to "web-ify" products and cross-sell offerings like home equity, car loans, revolving lines, etc. This all is a far cry than most bank's capabilities. Banks should first focus on delivering electronic capabilities to their current customers and streamlining their experience. Taking account documents online remains a challenge for 96% of independent banks, but must be done before even thinking about starting an internet-only bank. Online statementing, transaction capabilities and interactive marketing are all required. Since the success of internet-only banking is more about rate than anything else, most banks would do well beefing up their service offerings on their current internet site or speed their remote capture initiative to market, as both are more lucrative investments. This foundation will help gather less rate sensitive customers, while giving banks needed experience in channeling their customers. For internet-only banking, speed to market is less important. Getting internet-only banking customers back is easy since all it takes is 7 extra basis points to switch (the difference that most internet-only banking customers say it will take them to change virtual banks). However, if you are thinking long-term, offering both online capabilities and an internet-only bank will most likely be important over the next 10Ys. In the meantime, basic distribution channels can be further strengthened in order to optimize branch, phone and in-person visit connections.

BANK NEWS

MBA Index

Mortgage applications rose by 2%, due to higher refinancings (up 9.5%). Purchases fell by 3.0%. While down, recent lower rates should support the sector. However, with the current slowdown, housing will likely subtract almost 0.70bp from 3Q GDP.

Way Down

A monthly survey of CEOs finds confidence has fallen sharply and now sits at its lowest level in 3Y. Many executives complain that higher energy prices have also hurt profit margins. In addition, over 29% of CEOs said their company would likely reduce employment in the next 6 months.

Building Trend

A real estate research firm is reporting that a large backlog of condominiums has led 11% to 18% of the national construction pipeline to be canceled or shift over to conversion to apartments.

CRE Growth

The ICBA is reporting that CRE lending has equaled 67% of community bank asset growth every year since 2001.

Competition

JP Morgan Chase rolled out a new program called "Chase Freedom" which allows customers to choose cash or rewards on their credit cards. Specifically, the bank said it will provide larger rewards for customers that use their credit cards in certain stores.

Marketing

Wachovia reports the cost to attract new customers is more than 5x that of retaining them for the Bank.

Second Homes

A new study finds 2nd home sales increased 16% in 2005 over 2004, as the market share of 2nd homes overall increased to nearly 40% of all home sales.

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