

## DREAMING OF DEPOSITS

by [Steve Brown](#)

"If you snooze, you lose," may not be the best advice. Consider that if you don't get enough sleep, death will occur faster than if food is withheld. While no one is really sure what sleep does or how it works, we know it boosts human performance. Sure, sleep allows the body to rest, but so does watching American Idol. It is amazing that for something so important to the human condition, science knows so little about it. In similar fashion, deposit gathering is critical to bank performance. Yet, the industry is just starting to learn how to do it properly. While many bankers are familiar with deposit decay analysis, few are familiar with creation sensitivity. While deposit decay validation is important for asset-liability management, creation sensitivity is important in marketing. Like sleep, deposits must be gathered consistently and with quality to maximize performance. Left alone, deposits will run off. However, by proactively marketing, balances can grow. Creation sensitivity is the measure that translates each dollar of marketing expense (be it advertisement, sales salaries or free toasters) and rate, to deposit (or loan) dollar volume. By way of example, a bank in the Northwest rolled out their "Adventurer CD." This 2Y CD was promoted at a cost of \$18k that included displays, banners, in-branch promotions, a copy of a local guide to the outdoors and a drawing for a whitewater rafting weekend. At the time of the offering (several months ago) the rate was 3.50% when the median rate in the area was 3.25%. Over the course of the month, the program brought in about 70 new customers for a total of \$3.8mm in deposits. The creation cost for this program was marketing cost of \$18k plus the additional interest cost of 25bp (3.50% offering rate minus the median 3.25%) for total direct costs of \$37k. As a result, creation sensitivity for this was \$37k divided by 2 (years) divided by \$3.8mm, for a total of 49bp. To more accurately measure the cost, we would use present values and divide by the effective duration of the CDs (which is 1.81). We ultimately care about interest rate sensitivity, not time, but for the sake of illustration we are keeping things simple. What this means is that this bank used 49bp of "energy" to gain an incremental dollar of deposits. Please note that this is not a cost allocation exercise, as our calculation would have been different. The object here is to track how much marketing and rate it takes to pull in new money from the local community. Note that from a marketing standpoint, this calculation allows for easy comparison to wholesale sources, such as the FHLB or brokered CDs. In the wholesale arena, banks pay no marketing expense, so sensitivity is only the difference in interest rate. A rule of thumb to consider is that when local creation sensitivity exceeds the creation sensitivity of wholesale alternatives by more than 20% (which is a factor that represents brand building, customer cross-sell, etc.), then the bank should consider going wholesale in order to lower deposit costs. The calculation of creation sensitivity varies from bank to bank and promotion to promotion, but the idea is to track and monitor variable costs used to attract new money into the bank. By tracking sensitivity between rate and marketing (in addition to linking that sensitivity to different sales pitches), banks can gain a better understanding of what drives their community and how to more effectively attract deposits. Deposit gathering, like sleep, is crucial. To master both, consider tracking deposit creation as you dream up your next liability promotion.

## BANK NEWS

**M&A**

Susquehanna Bancshares (\$8.1B, PA) will acquire Community Banks Inc. (\$3.5B, PA) for \$860mm or about 1.67x book. The acquisition adds 80 branches to Susquehanna's network, primarily in central and eastern PA and northern MD.

### **FRB Warning**

A new report from the FRB warns that hedge funds may now pose the biggest risk of a crisis since 1998, when Long-Term Capital Management blew up. This is the FRB's strongest warning to date and is a result of detailed analysis the agency conducted on the \$1.4T industry.

### **M&A Study**

Experts say 50% of M&A transactions fail to increase shareholder value in subsequent years. Companies that exhibited the highest rates of success identified key employees within the first 30 days of the announcement, moved hastily to keep them and put these key players in positions that kept them motivated.

### **No Diversification**

Coast Bank of Florida (\$733mm, FL) reported a 1Q net loss of \$2.4mm, primarily as a result of an ongoing workout related to a builder that filed for bankruptcy. The Bank had loans out to more than 150 customers tied to this builder for a total of over \$100mm in credit exposure.

### **Bankruptcy**

April bankruptcy filings jumped 47% over the same month last year, pushing the 4 month total 63% higher than the same period last year.

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