SALE, SALE, SALE!

by Steve Brown

After-Christmas sales are almost as much a part of the holiday tradition as a tree and the carte blanche to grab some extra helping of Christmas dinner. However, running promotions aren't without their costs. Big discounts on services or products, either fees or rate, or high rate promotions on deposits all hurt a bank in several ways. Many of these ways we have written about in the past. Since we have covered why discounts/promotions attract the wrong type of client (those that value price before service) and we have said how promotions "train" customers to be more price/discount sensitive, we haven't covered how customers change behavior based on certain pricing techniques.

While big discounts/promotions can work wonders to increase production numbers in the short-term they also can hurt the image of a bank's brand. New research shows that discounting goods can lead consumers to expect permanently reduced prices, which in turn can stifle sales when the items do return to full price. While you might have purchased something for yourself over the last several weeks, most shoppers will wait to take advantage of the after Christmas sales thereby hurting a store's margins.

For those that do want to run product discounts or promotions, we offer some tips on how to maintain profitability culled by the latest research and bank experience. For starters, if you are going to advertise a promotion, saying something is "free" rather than "reduced" erodes brand value the fastest. Once customers know that you are willing to give something away, it is hard to get them to ever pay full price for that item again. Remember, "Free Checking" started off as a promotion and is now a permanent fixture in banking.

Another idea is if given the choice between expressing a discount as a percentage or a dollar discount, choose the dollar discount. Percentage discounts, such as "Open an account and we will reduce fees by 23%", isn't as memorable as, "Get $9 off fees when you open a New Saver's Bundle." For similar reasons, hard-to-calculate discounts like 19% do not drive down consumers' price expectations as much as simple discounts like 25% or 50%. The take away here is that banks should stick to dollar price promotions unless they want to tout a large, whole number percentage discount. Here the research shows that both can be effective.

Finally, the best advice on sales from top performing bankers is to know what you are doing. All sales and price promotions hurt a brand to some extent. That said, they promotions can be profitable. The trick is to understand how a promotion will affect future profitability before you run them. The more price sensitive the customer, the more a promotion will drive sales. In these cases, profitability is easily measured since a promotion will cause a higher dollar volume of sold product, just at a lower margin. For low price sensitive customers, a promotion may not drive volume and will only end up hurting the brand in the long-run. If you are going to run a promotion, here is the simple rule of thumb Â– if you are prepared to monitor, analyze and learn from the promotion - go for it. Any value lost in brand or margins will hopefully be made up in educational value. If you are not prepared to be quantitative about your price promotions, then stick to marketing on service only. This will not only give you a far smaller chance of hurting your bank's brand, but it will also allow your shareholder's to gain a little extra return to take advantage of other retailer's sales.

BANK NEWS

Fed Funds Futures

The odds of a 25bp ease in January stand at 75%, down from 100% last week.

Zions

The bank will take a $94mm write down due this month to its debt exposure associated with REITs, residential mortgages, securities and home builder loans.

Bank Failure

The FDIC proposed a 2-part rule that is targeted at improving the process for uninsured depositors to get a settlement in a large bank failure. The proposal requires the 159 largest institutions to have a process and systems in place to place/remove temporary holds on certain accounts and generate deposit reports in a standard format. In addition, all institutions will be required to be able to generate end-of-day ledger balances with enough information (account type, holders, amounts, etc.) to determine the time and circumstances which balances would be closed in the event of failure. The comment period is open for 90 days.

Subprime Clean Up

As expected, the Fed proposed new rules to curb subprime mortgage origination problems. The proposal includes a prohibition against lending without the review of a borrower's ability to repay (funny isn't); bar loans based on unverifiable assets; require an escrow account for taxes/insurance; and, permit prepay penalties only under certain conditions. In the future, the mortgage industry should shut the barn door before the cattle have all fled.

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