THE FUTURE OF REMOTE DEPOSIT CAPTURE

by Steve Brown

As we travel around talking to banks, we notice two things that have transpired since 2005. One, hotels have removed all their light bulbs. Our stay here at the 'W' hotel brought this home, as the place is filled with good looking, 20-somethings all wearing black. Apparently, light is now un-hip. This is a problem, as it leads people to run into each other in the hallways (see picture). Forget candy bars in the room, we would pay $20 for a flashlight.

The other thing that has happened since 2005 is the rapid adoption of remote deposit capture ("RDC"). While we are often critical of our industry, one thing that we are proud of is the speed at which community banks have adopted RDC. In just a little over 3Ys time, more than 80% of banks now offer the product to their commercial customers. The question now is what comes next?

One answer is to start to focus more on relationship profitability. About 50% of the banks we talked to have expressed the point of view that RDC is not living up to the hype. We disagree and point out that the real savings will come from the reduced number of branches banks will have to build in the future. In addition, the product opens up a strategic direction that wasn't available before. For instance, a bank in FL has a specialty of banking self-storage centers across the country. This specialty is only made possible by RDC and online banking.

While it appears only about 15% of banks give away their equipment and service for free, how banks charge or what they charge has little correlation to profitability. While fees are never bad, the most important driver of profitability is the type of account. To increase profitability, banks should figure out what types of accounts are working for them and then expand on that success.

When going after a particular account segment, we have seen profitability across a wide spectrum (so we can't, give you a list). Liquor/convenience stores, non-profits, municipalities and title companies all fall in the above average category. A general rule of thumb is to target small business with over 25 employees that receive more than 50 checks a month. However, this is a little like having a dark room - it is hard to see the whole picture.

In 2008, banks have begun looking at a mix of median check value, velocity of flow and number of checks per month, to tray and determine RDC installation profitability. A small business that processes only 30 checks a month with a slow production turn and a median check value of $700; is much more valuable than a business that processes 200 checks per month, at a median check amount of $75 and has a high velocity of flow. One bank hit the jackpot when it sold RDC to a manufacturing customer that used portable scanners with its sales force. This customer's sales staff was able to accept orders and checks at the point of sale for the first time, instead of creating a receivable and waiting to receive payment. The manufacturer not only increased its business because of ease of use, but it was also able to shorten delivery times. The bank was also a winner, as it increased its deposit base by $3mm for this particular customer.

The takeaway here is that while many types of accounts can be profitable, your first focus should be on larger business-to-business accounts, instead of those with a retail focus.

After conquering the profitable customer segments, another strategy that banks are starting to implement is to go after the smaller business (those with less than 25 employees). This opens up some 22mm businesses across the U.S. To do this, some banks are turning to the use of the customer's own flatbed scanner (80% of small businesses have them) and internet-based software to accept scanned images. This drops the cost and removes much of the servicing burden from the bank. Professionals, home-based product sellers, trade businesses and retail accounts now can all become profitable.

In an effort to shed more light on RDC profitability, we will pick this up again tomorrow - that is, assuming we can find the door to the hotel room.

BANK NEWS

Lost Deposits

Get this - Starbucks now has $1B on their prepaid cards. That is $1B not in the banking system. No wonder deposit rates are so high.

FDIC

The Deposit Insurance Fund raked in $2.2B for 2007 (up 38% from 2006), increasing the fund balance to $52.4B.

ID Theft

The FTC reported that ID theft was its biggest consumer complaint in 2007 (for the 7th year) composing more than 32% of all filings. Credit card fraud, utilities impersonation, employment fraud and bank scams were the largest categories of ID theft complaints (in order).

CRE Concentration

The OCC reports that more than 60% of community banks nationwide have CRE concentrations that exceed 300% of their capital and about 30% have construction and development loans that exceed 100% of capital.

Business Customers

A new survey of small business owners finds 87% do not plan to fully retire from their company, 43% do not think they will have enough money to retire, 69% say they will travel more, 84% will pursue personal hobbies, 17% will move to another state45% think their business will be run by a family member.