THE HAWTHORNE EFFECT AND GOAL DRIVEN SAVINGS

by Steve Brown

They call it the "Hawthorne Effect" and it is the hottest trend to hit savings accounts since reward points. In 1924, a company that produced telephones commissioned a study to see if different levels of light affected worker productivity. As expected, the workers with higher levels of light performed better when compared to the workers in a normal environment. While not ground breaking, it wasn't until 1955 that organizational psychologist Henry Landsberger reviewed the results and found that that something else was going on. He postulated a theory that it wasn't the extra light that increased productivity, but rather the mere act of observing workers that increased output. When someone else cared, Landsberger reasoned, people performed better. This "Hawthrone Effect" has been studied in various human endeavors, from relationships to athletic performance. It holds that human performance is often more efficient when measured. In fact, as a rule of thumb, the Hawthrone Effect is said to account for 15% more productivity on average. While the theory is controversial, we are believers and see evidence of this effect when it comes to savings accounts.

Banks report an increase in balances between 5% and 20% when a savings account is opened for a specific purpose, the account holder sets goals and those goals are reinforced. PNC Virtual Wallet is an example of this, which we have widely written about in the past. Now, Citizens Bank ($136B, RI) has rolled out a series of accounts that take advantage of the Hawthorne Effect and the recent trend of increased savings.

Citizens' HomeBuyer Savings account allows people to earn $1k, if they make a minimum of $100 per month deposit for 36 months and then purchase a mortgage through the bank. This account currently pays 30bp for balances under $1k, 40bp for balances over $1k and 50bp for balances above $2.5k. The account not only motivates larger balances through positive reinforcement and goal-oriented savings, but the duration of deposits is dramatically increased because the structure penalizes the holder (by removing the $1k reward), if they miss more than 1 month per year of minimum savings.

Citizens smartly also extends this same structure with its College Saver account introduced earlier this year. Here, account holders can earn $1k if an account is opened before a child's 6th birthday and maintained at $25 per month until they are 18. Current rates are the same as above, with the top tier placed at $10k. For those wondering why the top tier for the College Savers account is at $10k verses the HomeBuyer account at $2.5k, the answer is Citizens has brilliantly segmented their customer base. Households that are saving for homes are almost 2x as sensitive to deposit interest rates than college savers. As a result, the College Savers account is more profitable (even with the profitability of the mortgage included) and due to its structure, also has a longer duration.

There are many variations on this theme that banks can take advantage of. It starts with a niche savings product, with the right structure, backed by a little technology (so that account holders can chart their progress online and receive periodic e-mail or text updates). This type of account is sure to be a winner in the next several years while households are focused on savings. Travel, vacation homes, business equipment, retirement, weddings or other savings goals can be articulated and marketed in a segmented fashion to increase profitability.

BANK NEWS

Transaction Acct Guarantee Extension

The FDIC is meeting today to decide whether to extend the unlimited guarantee on noninterest bearing transaction accounts above $250k for another 6 months or perhaps a year. Expectations are that the guarantee will be extended, but the fee will rise from 10bp to 25bp. Note that standard deposit insurance coverage of $250k is good through 2013.

Suspended Dividends

The WSJ is reporting that 3 banks have suspended dividend payments to the Treasury under TARP, as they scramble to shore up capital. The banks were reportedly Pacific Capital Bancorp ($9.2B, CA), Seacoast Banking Corp ($2.3B, FL) and Midwest Banc Holdings ($3.7B, IL). In total, TARP capital has been injected into about 600 banks nationwide.

Crackdown On 3rd Party Deposits

Regulatory agencies issued a new regulation requiring banks to monitor deposits received through third-party referrals, particularly related to above-market rates; have controls in place to flag unusual deposit activity; understand the definition of a deposit broker; record deposits received by any broker as brokered deposits; reminds adequately capitalized banks that they cannot accept or use third-party referral deposits and reminded banks that third party deposits are considered volatile.

Loan Loss Reserves

Last week's regulatory overhaul proposal by the Obama administration includes wording telling FASB to improve accounting standards for loan loss provisioning by the end of this year. Experts say the change is designed to allow banks to put away more reserves when times are good to prepare for when times are bad.

Credit Crisis Tally

The IMF projects worldwide losses form the credit crisis will reach $4.1T by the end of 2010.