PRIVATE BANKING & RELATIONSHIP PROFITABILITY

by Steve Brown

We have a client bank that has rolled out a series of loan, deposit and cash management promotions around the upcoming World Cup Soccer tournament that starts this week. The game will be played on all branch plasma screens and marketing pieces will discuss teams and current standings. There will be a

soccer ball giveaway for the kids, T-shirts for the adults and a product promotion that waives fees for some products during the tournament every time the US wins a game. The marketing effort reportedly triples branch traffic (they have done something similar in the past) and increases both loan and deposit production by an average of 8% for the month. Today, the bank will be holding a separate drawing for registered private clients that will give away a trip to South Africa.

The promotion got us thinking about the nature of private banking. There is a myth in banking that having a special department or division that caters to the wealthy or affluent customer is profitable. The fact is that by looking at our Relationship Profitability data, this is no more profitable than other mainstream lines of banking (about 65% of high net worth clients are profitable over the last 10Ys). In other words, the distribution of profitable departments almost mirrors that of the banking universe.

The reason for this is two fold, pricing and client management. Banking the high net worth set should be profitable, as the group carries larger balances and utilizes more products of a community bank, despite also having more banking relationships. When it comes to pricing, banks often assume that wealthy clients are much more price sensitive than they actually are. As a result, these clients are usually given the highest rate on all of their accounts, when they don't require it. What wealthy clients need, according to surveys, is superior service and constant access to their money. Banks shouldn't confuse service with rate. Loan and deposit rate methodology should be the same for wealthy clients as it is for mainstream ones.

The irony of private banking is that it often results in profitable customers being moved into a special department that entitles them to greater customer service and benefits. This process turns once profitable customers into unprofitable customers as costs are increased. In addition, one of the great myths of private banking is that these customers are also the best ones to cross- sell. This may be true in theory, but if private banking customers are unprofitable in general, they are most likely also unprofitable along additional product and service lines. Among the well-heeled, there are some customers that will squeeze every dime of value from an institution, while others are competitive and still others are highly profitable. Many banks make the mistake of assuming everyone in their private banking division is a sought after customer. Surveys reveal that very few customers are ever removed from private banking groups once they are admitted, including at many of the major banks. Statistically, this should not occur, proving that few banks actively manage group profitability.

For some banks, customer profitability automatically places one in the "VIP Division," irrespective of net worth. This is an interesting approach and tends to help retain and manage the 10% of bank clients that drive profitability.

For some banks, having a private client group is a necessity (due to the competition or demographics composition of the service area); while for others it is a method of diversification or a marketing tool. Private banking can work, but the basic rules of customer profitability and marketing still apply. For the division to be profitable, intelligent pricing and proactive client management are the keys to ensuring success. Unfortunately, we are less optimistic about the US's upcoming game with England, but we are keeping our fingers crossed.

Related Links:
BIG Metrics

BANK NEWS

Closed (84 YTD)

The FDIC closed: 1) First National Bank ($60mm, MS) and sold it to The Jefferson Bank ($55mm, MS). Jefferson will receive 1 branch, all deposits (no premium) and all assets ($44mm under loss share). 2) A buyer could not be found for Arcola Homestead Savings Bank ($17mm, IL), so the FDIC will pay out all insured deposits. 3) TierOne Bank ($2.8B, NE) and sold it to Great Western Bank ($5.6B, SD). Great Western receives 69 branches, all deposits (1.5% premium) and most assets ($1.9B under a loss share). For more information, follow the BIG Metrics link in our related links section below.

Bank Size

Dallas Fed President, Richard Fisher (non-voter), urged fellow regulators to institute a maximum asset size for banks in order to prevent the too-big-too-fail syndrome. While Fisher didn't say what that cap might be, it was speculated that $1T might be the limit that would impact 4 banks that are over and a group of banks that are approaching that limit.

Online Fail

A Javelin Strategy & Research report noted about 25% of adults in the US attempted to open an online account this year. However, more than 50% of those were unable to open and fund a checking account. Over the last 2Ys, fewer and fewer consumers have tried to open online accounts according to the data.