THE DISTRIBUTED PRESENCE BANK MODEL

by Steve Brown

What is your distribution strategy? That is, how do you plan to provide service and products to your customer base in order to efficiently gain deposits, fees, loans and satisfaction? If that question only makes you think of your branch network, you are in trouble. If you are thinking about branches and your website, you are still in trouble. Over the past 2Ys, what is showing signs of success is what we term the "distributed presence model."

First let's talk branches. The traditional, large branch for most customers is almost a joke from a profitability standpoint. Most branches are capital intensive, costly, inflexible and present a low return. When we look at bank profitability data, it is almost too easy to prove that banks are paying their customers to do business with them. Look at customers that utilize your branch and it is most likely the bottom 60% of your unprofitable customers. In short, you are paying customers to do business with you through this channel.

A better way to deliver products and services is a multi-layered approach. While large branches are still important, they are not critical to delivery and are deemphasized. Let's take an example utilizing a $2B institution with 41 branches. This is far too common, but 73% of these branches (about 30) are unprofitable and will remain so until short-term rates go above 3.00% (which could take a couple years). Even after that, nearly half will remain unprofitable. For this bank, it might make sense to close 25 strategically unimportant locations and open up 5 store front branches. Then the bank could run promotions to incentivize the impacted customer base to use one of the remaining delivery channels, making remaining branches more profitable. At the same time, we would suggest the bank consider replacing some of the service areas with imaged ATMs and probably augment with a loan production office or two. We would then recommend investing $1.5mm in a more robust technology platform that allows account opening, wires, alerts, statementing, currency ordering, mobile banking and international services, in addition to the standard online banking/bill pay (at a minimum). We would then suggest increasing the development and use of both RDC and remote cash capture to handle business needs; as well as rolling out RDC for retail. In addition to all of the above, we would suggest the bank consider boosting its social media presence for good measure.

Lease termination costs aside, this bank would end up with a more efficient platform that is a mix of traditional branches, smaller offices and technology. The structure would allow the bank to service more customers at about 30% of the cost. Instead of spending $4k dollars on average to service a customer for the year, the cost drops to $1,700. The funny thing about all this is we also would bet customer satisfaction would rise, as each customer has more options than before through a greater range of delivery channels.

We are not saying the above is the answer to getting your bank a lower efficiency ratio, but it is one possible answer. We remain convinced that the future of banking is a multi-layered approach to channel delivery, with a greater emphasis on smaller store front branches, ATMs, mobile banking and online technology.

As banks struggle for profitability, this structure is also cheaper, less capital intensive and multiple times more flexible. While politics, regulatory realities, lease terms and competitive factors will surely get in the way, our point is to get community banks thinking about reducing their infrastructure cost, because it is eating many good banks up alive.

BANK NEWS

Capital Regulation

The chief national bank examiner for the OCC said risk-based capital standards represent minimums, suggested banks rely more on their own ALLL analysis than rely on accountant advice and pushed to increase capital buffers for banks that have concentrations over certain levels in commercial real estate. He said bankers should expect regulators to require higher individual capital levels based on specific facts and circumstances. He indicated the OCC will require this where they see significant CRE concentrations.

On Again

The Senate has agreed to once again consider the small business legislation proposed last year. The legislation would ease terms for SBA loans, provide $12B in tax breaks to small businesses, issue grants to states the support business lending and deliver $30B in capital to banks with less than $10B in assets (that would be priced on a declining basis depending on the amount of small business lending the bank does). A vote on the bill could come this week.

Strategic Planning

Bank of America has laid out a strategic plan that relies less on acquisitions and will focus on cross selling and pruning its balance sheet. The Bank is reportedly working to identify up to $100B of assets to sell in order to shrink its balance sheet; will close branches; lay off workers; raise deposit minimums; raise monthly fees; maximize the number of products/services sold to each customer and try to push even more customers to use automated channels.