

BUSINESS CHECKING ACROSS AMERICA "PART II"

by [Steve Brown](#)

Yesterday we highlighted business checking, particularly ideas for a basic and mid-tier account offering. Today, we had planned on further analyzing checking, as well as premium checking accounts. However, since we received so many questions and comments about our article yesterday, we thought we would put the topic of the two other checking types off in order to step back and highlight a couple of points in our account design discussion.

We want to clarify that we are only presenting ideas based on the average community bank. Each bank obviously needs to decide for themselves, based on the markets they face and their goals, what works best. There are regional differences driven by competition, demographics and other factors. For example, fees can be about \$5 per month higher in the Northeast compared to the South. In addition, if a bank has a goal of capturing both the business and the retail account of its owner, pricing can be adjusted downward, as profitability is increased (but so is focus).

We also would like to clarify that we are just talking about account basics here. We are strong advocates of adding bells and whistles, such as fraud protection, international payments, waiving foreign ATM fees and the like; as each may increase duration, convexity and help marketing. However for the sake of space, we were seeking to keep things simple.

Yesterday's article also generated a lot of questions regarding profitability. Some bankers pointed out that we recommended too low a minimum (\$500) and too high a maximum free item number (250) for the value on the mid-tier checking. These bankers could be right, but our argument rests on a couple of items worth highlighting. First, the value of the account is largely driven by the duration of the balances and the convexity therein. The reason the business checking account is one of the most profitable products in banking is due to the high balance, non-interest rate sensitive nature of the funds. This extends liability duration, giving the bank economic value when rates go up. Further, the account exhibits extreme positive convexity, so economic value increases, at an increasing rate, when rates rise. Here, not only does the bank gain value when interest rates increase, but balances also tend to increase, given increased profitability at the business client themselves. Conversely, when rates fall to a certain level (the bottom quartile of historic rates), balances increase, offsetting some value in a falling rate environment. This is also why online banking, bill pay and mobile banking are so important. While a cost, these more than pay for themselves by increasing retention, duration and convexity.

Finally, we received many questions on setting account minimums. Setting minimums is one of the most important aspects of account design, as the moment you do, you improve value (most deposit balances are normally distributed). When you introduce a minimum, the distribution shifts around that minimum, to what is called a "splice distribution." This skew is a result of accounts wanting to hold higher balances in order to save on fees. The trick with setting an account minimum is to elicit the greatest shift in economic value as possible. Set it too low and the shift isn't great enough to offset the loss in fees. Set it too high and customers move to a different account.

If you would like to learn more about account structuring, rate setting and new products, we will be having multiple sessions on these topics at our upcoming Executive Management Conference starting May 18th thru the 21st in San Francisco. To learn more and to find an agenda, pricing and registration go:

<http://www.pcbb.com/conference.html>

BANK NEWS

4Q Earnings

Bank of America reported a \$1.24B 4Q loss, as it increased loan loss provisions, boosted legal reserves and booked \$12.4B in 2010 impairments on credit card and mortgage units. SunTrust reported a 4Q profit of \$185mm, driven by lower loan loss provisions (down 47% from 2009); lower net charge offs; and reduced non performing loans. The bank reported loans fell 0.9% during the quarter, while consumer and commercial deposits increased 2.3%. BB&T reported 4Q profit of \$208mm, beating expectations. Performance was driven by lower loan provisions (down 11% YOY) and a slight increase in loan balances (0.9% increase).

M&A

People's United Financial (\$20.4B, CT) has entered a deal to purchase Danvers Bancorp (\$2.6B, MA) for \$493mm, following 2 other acquisition deals announced in July.

Finally

Now that Dodd-Frank Act has permanently raised insurance-coverage to \$250k, the FDIC is indicating amounts between \$100k and \$250k won't be treated as "non-core" for Call reporting purposes.

Mega Deposit

A bank teller from Idaho has officially claimed her half of the 2nd largest lottery jackpot in history. Holly Lahti is the winner of the \$190mm Mega Millions pot and the ticket was purchased in Post Falls, ID (no word on what bank she worked for, but we'll keep checking around).

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