BANK MERCHANT REWARD PROGRAMS

by Steve Brown

At our upcoming EMC Conference, we will be discussing new products that help banks generate more fee income. One such product that is catching on at community banks are merchant funded reward programs.

A merchant funded rewards program plays off the current Groupon / Foursquare trends and combines it with the need for banks to generate more debit transactions, post Durbin. Similar to a bank-funded rewards program (which we have long been in favor of), a merchant program shifts the cost rewards points to a merchant in exchange for transactions. Instead of the bank tracking and funding points for deposit balances and debit card usage, customers that purchase goods and services through a branded web portal are rewarded. Bank customers register their debit card numbers with the bank and are then presented offers via online links, mobile apps, e-mail or other channels. Users are offered discounts and make purchases with their debit cards. Merchants then leverage these sales and pay a fee (typically 5%) so that the bank can return cash (good) or reward points (better).

Several turnkey vendors exist to make it easy for banks and the path is now well worn, with approximately 750 banks offering this product (including most majors such as BofA, Chase, Citi, etc.).

The downside to instituting a merchant rewards program is that customers may feel over marketed - diluting the bank's efforts in other areas and creating additional "noise." In addition, local merchants might get upset, as nearly all of the participating merchants are national in scope (such as Target, Sears, Macy's Office Depot, etc.), thereby potentially infringing on local sales.

However, if you can control the program and mitigate the downside, community banks may find these programs valuable. Many banks find that 8% to 25% of their customers take advantage of the program. Depending on how the program is set up, banks can share in advertising revenue, debit card usage interchange, more online banking transactions and more overall general bank website traffic. In short, the program is a tool to tie the bank closer to its customers, aiding in retention and new customer acquisition.

While by no means definitive, our cursory review of some banks performance did show traffic on the bank website increased by some 5% (visits per month), the average customer purchased about $50 of goods per month, netting the bank $5 in rebate/rewards to potentially pass on to their customers. For those customers, debit card usage increased by about 18% and roughly 20% of the customers that were inactive became active (which is a step in the right direction when trying to make unprofitable customers more profitable). All told, the estimated value of a program like this comes to about $38.64 per year per customer, not including the cross-sell aspects, increased retention or acquisition.

If you are looking for ways to become more relevant to your retail and small business customers, while increasing fee income, a merchant funded rewards program should be considered. These programs cost very little to launch, save for some management, IT and marketing effort and can be brought to market in under 60 days. Be sure to attend our New Product discussion at our EMC Conference where we will evaluate different options banks have for getting involved.

BANK NEWS

1Q Earnings

JPMorgan reported a 67% increase in 1Q profit, as credit quality improved and activity at its investment bank increased. On the bad news front, JP said its retail-services business, which handles consumer and small-business clients, suffered a worse loss than the same period last year, as it took hits in its mortgage business and small business loan growth fell 8% from the prior year. Meanwhile, the bank reported 5% loan growth to businesses with revenues between $10mm and $500mm. Finally, improved asset quality pushed provisions for credit losses down 83% to $1.17B, down sharply from the $7.01B level of last year and $3.04B in the prior quarter.

Waiver

The FHA has approved a waiver of the audit requirements for FHA direct lenders that have assets under $500mm. The audit requirement went into effect in Jan and began affecting lenders on Mar 31, following a 90-day grace period. The FHA will issue a letter with the waiver's details, which are expected to allow banks with assets $500mm and below to submit Call Report data instead of an audit.

BofA

BrandFinance recognized the Bank as the most valuable banking brand in the world. In other news about the Bank, it launched its "Project New BAC" which is a targeted internal effort to increase efficiency by boosting retail customer revenue, cutting loan approval times while reducing expenses.