TEXTING AND M&A IN BANKING

by Steve Brown

You might be shocked to find out that the average person who sends text messages pay $1,250 per megabyte. That is because text messages max out at 160 bytes and at around 20 cents per message that becomes quite pricey. Research also finds that only about half of people use a bundled plan. Maybe that is why the wireless industry makes 80 cents of profit on each dollar they make from texting, according to the WSJ. People don't think about this very much, but the next time a customer gripes about ATM or other fees your bank charges, you might want to compare it to the cost of texting. Whatever you charge at your bank will seem very inexpensive in comparison.

That got us thinking about the cost of M&A. Given the burden of Dodd Frank, exhausted directors and management teams that have been fighting credit issues, increased regulatory scrutiny and a difficulty in making money overall given the business model, more banks are talking about M&A these days. Since that is the case, we thought a refresher of a few things to consider around this subject might be in order.

First, know that research by McKinsey finds the size of the deal does not matter when measured by total return to the shareholder. Statistically speaking at least, researchers found the performance is about the same, whether a company does one large deal, multiple small deals or just a handful of deals. That means the number of deals or size of them means a lot less than spending time to find the right partner, pricing the transaction properly, integrating it effectively and managing through customer attrition and other issues.

Next, researchers that examined thousands of mergers found successful ones should be strategic. While many banks say buying the bank next door is strategic, the data shows key drivers typically sought by the acquirer focus on improving performance of the company they are looking to purchase; acquiring skills or technology faster than they can be otherwise built in-house; deepening product sales opportunities through an expanded customer base and removing excess capacity from the industry. According to the research at least, if the deal does one of these things, it stands a better chance of delivering value.

A third consideration that banks in acquisition mode should think about relates to market consolidation. If the game is to buy other banks so prices can eventually be raised, it is important to know that the research also shows this is usually only effective when the consolidation cuts the number of players in a given market down to four. Given the general competitive landscape, bank competition from non-bank sources and the power of the internet, gaining some form of pricing power is difficult.

Finally, make sure you carefully consider the culture of each bank target before you get too emotionally involved in the deal. Nothing makes a deal blow up faster than when the culture of the two banks clashes. Before you start looking, determine the key values you are seeking and compare your bank to any potential purchase to be sure the culture fits your own. Does the bank in question truly have a client focus, do they work well in a team environment, how well do they adapt to change and other factors all need to be considered before you text "done" to your board. If your two-column analysis sheet of "us" and "them" doesn't match up very well, walk away and keep looking. You will retain your sanity, your franchise will remain a franchise, employees and customers will be happier and you will eventually find a partner where your services can be bundled with theirs to achieve better long term performance.

BANK NEWS

M&A

Capital One will buy ING's online bank for $9B in cash.

HSBC Branch Sales

The Bank continues its retreat from retail branch banking as it puts its 175 branch network in upstate NY up for sale. Bids are due Monday and deposit premiums are expected in the 4% to 6% range.

Bank CEO Pay

US and European large bank CEO pay increased an average of 36% to $9.7mm for 2010.

e-Statements

In a trend we highlighted last month, we note that Wells, Zions and several other major banks are all running incentives this month to get customers to switch away from paper statements in order to save costs.

CD Rates

The average retail CD rate in the nation was 76bp (irrespective of maturity) largely unchanged from last month. AK, ID and OH have the lowest rates by state, while IA, MS and NJ/VA (tied) have the highest.

Green Branches

TD Bank was curious if having a "green" branch was worth the extra cost in terms of marketing. A poll of consumer awareness showed that 75% of potential customers thought green buildings have at least some impact on the environment. However, only 33% of the respondents knew which buildings were "green."

Reverse Mortgages

Wells Fargo joins BofA in exiting the reverse mortgage business (and will layoff 1k workers). Falling housing prices, greater consumer compliance and more media attention on foreclosures have made reverse mortgages a riskier proposition. Wells was the largest such provider in the market at $4.7B (1.2% of its total mortgage book).