

## Take Care of Your Nose

by [Steve Brown](#)

There was a romantic Ukranian author named Nikolai Gogol who lived in the first half of the 19th Century. Whether you heard of him or not, note that he was one of the first masters of the short story along with Pushkin and Edgar Allen Poe. While considered a romantic, Gogol often foreshadowed more cynical literary styles like satire that mostly would not flourish until a few decades later. One odd surrealist short story is called The Nose. In the story, a self-important military Major wakes up one morning to find his nose missing. The major's nose has decided it would rather go it on its own and begins acting as a human. Soon the nose achieves a higher rank than its former owner and logically refuses to return to the major's face. In the end the nose returns and all ends well - very weird.

We are not completely clear on the deeper meanings of this story, but we are aware of banks that are considering parting with their own noses by choice, without a lot of thought on how this could affect the health of their bank. Without a nose, it's hard to smell opportunity or sniff out risk. We point out that many banks are in the process of doing their budgets and are looking for places to cut expenses. This is great and from time to time it makes sense, but there are choices to be made on where to cut and this is the tricky part.

We would like to make some suggestions regarding assessing which services to keep, those to cut and those to reduce. There are expenses tied directly operations, technology and personnel - there may be reductions to be found in this category though it is often one of the most difficult. There are those tied to business development, marketing and outreach. No easy choice there either, as marketing is your bank's brand. Finally there are those expenses that are tied to making banks operate more efficiently and offering performance enhancements. These would include loan pricing models, strategic and liability consulting, management tools like outsourced ALM and ALLL or stress testing of the loan portfolio. These types of services help banks measure and report risk, price loans appropriately, strategically manage their products and sales practices, so they are very risky to cut. Certainly, while this last group have costs, before considering cutting, it's really important to accurately measure if compliance functions can be done more efficiently in-house. Additionally, consider whether the performance achieved through the use of quality consultants can be continued without the assistance of outside experts.

Since this is such a key consideration for banks, we provide a real life example offered by our strategic coach service. For a bank with \$100mm in assets, a single 1bp in lower funding costs can save a bank \$10,000 per year. That reduction in funding costs also makes the bank better able to compete for loans and is likely to reduce interest rate risk. The key to reducing expenses is to look at the value each one is delivering. If it more than covers its costs, then move to the next one and repeat the process until you find one that doesn't. In this way, you will give your bank every advantage, while keeping in place those services that are adding positive value.

The next time you think fees have gotten out of hand and you are paying through the nose, be sure to carefully analyze what a given product or service does for your bank. It will ensure it is not cut off to spite your face.

## BANK NEWS

## **Economic Expectations**

The Fed just updated its economic projections for 2014 saying it expects the unemployment rate to be 6.3% to 6.6% vs. its last projection of 6.4% to 6.8%. For GDP, the Fed expects 2.8% to 3.2% growth in 2014, vs. 2.9% to 3.1% prior.

## **Swaps**

The CFTC estimates the swaps market is now \$390 trillion in notional size.

## **Mobile**

Studies find 43% of emails are now opened on a smartphone or tablet.

## **Improving**

Zillow reports home values jumped \$1.9T this year, marking the largest move since 2005. Despite the increase, values have only recovered 44% of the total lost since 2007.

## **Big Change**

comScore reports that for the first time ever online sales have blown past the \$1B mark as sales are up 21% so far this year.

## **Busted**

James Ladio, the founder and former CEO of MidCoast Community Bank (DE), has pleaded guilty to charges of bank fraud and money laundering. Ladio reportedly admitted he got customers of the bank to apply for loans and then wire money to him.

## **Marketing**

Banks wondering where to spend marketing dollars in 2014 should note Google and Nielsen find 73% of mobile searches result in additional action taken and 55% of purchases happen within 1 hour of an initial search.

## **Customer Change**

A new Fed study finds about 20.8B more electronic cash payments occurred in 2012 vs. 2009 (up 8.3% annually), as people continued to change behavior from paper to electronic methods.

## **Regulatory Warning**

The OCC has released its top risk challenges banks will face in the coming year and says they will be low yields on investments, rising cyber attacks and low returns. The OCC warned banks to be careful when moving into new products in search of revenue as they may contain unfamiliar risks.

## **Fined**

Deutsche Bank will pay \$1.9B to settle FHFA claims related to mortgages the bank sold FNMA and FHLMC from 2005 to 2007.

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