FEATURE STORY

Customer Profitability - From Strategic Development to Execution

By Earl Charneske

As the economic environment continually changes, developing bank-wide strategies to grow profitability while mitigating risk can become more difficult. However, that is when it becomes even more critical.

Strategic Development

Start by developing strategies directly related to the efforts of frontline staff since this is where you can influence your customers most directly. It is an informative exercise to review existing profitability and risks of current product lines, customer segments (industry type), markets, and relationships while considering the impact of potential changes from the economic cycle. Some questions to ask yourself and others include:

What is driving the current and long-term profitability of the bank's product lines, customer segments, markets, and relationships?

If future conditions change, how will the bank's strategy change?

These questions and more should be addressed thoroughly.

While you may think that you have a pretty good handle on all of this already, we have found that bankers may have a slightly different perspective than the profitability data reveals. While you may know your customers well, you also may give them the benefit of the doubt in some situations, without reviewing the full customer relationship. The right strategies will put you on the right course.

Some Strategies to Consider

1. Prioritize highly profitable segments and understand key drivers impacting current and future returns
2. Identify the bank's top customers and review retention programs
3. Evaluate product pricing, based on each product's relative value to the bank and the opportunity to strengthen profitable relationships
4. Review opportunities for cross-selling by product and impact on revenue, with current and changing conditions in mind
5. Identify lower-performing relationships and pinpoint opportunities to improve returns
6. Target marketing efforts by profitability potential, relationship and customer segment
7. Align officer performance tracking with incentive plans

As you develop these bank-wide strategies, think about including a larger breadth of officers from other departments, especially those closer to the front lines. Not only could they provide additional insights, but it could also facilitate a smoother execution process.

Strategic Execution

For the execution of your strategies, you will want to include four main components: communicating the goals; achieving goals; tracking and measuring success; and providing pathways for peer review and feedback.

1. Communicating the Goals

The management team should provide clear communication on what the goals are, how they apply to the frontline officers individually or by team, and how they impact the end customer. This way, everyone is on the same page.

2. Achieving Goals

The strategies devised by management are a means to achieving higher profitability. However, there are many ways to meet the end goal. Sharing the insights and findings from your strategy review with your teams will not only give them a starting point for action, but also inform them of new ways to approach their goals. With that said, allow officers some freedom in how to achieve these goals, so they have a sense of ownership. There are more ways than one to make existing relationships more profitable. For example, consider reducing costs by consolidating underutilized accounts or cross-selling services to not only increase fee income, but also increase retention.

When evaluating existing relationships and pricing new accounts, providing the means for officers to review the impact of varying factors (changing terms, rates, deposits, fees) on risk-adjusted return is integral to this ownership process. Furthermore, it ensures higher returns are not coming at the cost of accepting unreasonable interest rate or credit risk.

3. Tracking and Measuring Success

Does achieving the goal equate to a positive impact for the officer? Or does increased profitability for the bank mean higher compensation or value for the officer?

Officer compensation plans should include profitability as a measure. So, it is important to design these measures to be concrete and transparent to ensure alignment with officer behavior. Track each officer's portfolio profitability as a whole, as well as new accounts only, over a rolling period (quarterly, semi-annually, etc.) and by total new volume. In this way, officers will be encouraged to bring in volume growth and higher risk-adjusted returns.

4. Providing Pathways for Peer Review and Feedback

Once you have the right tracking and measuring tools in place, you will want to create a channel for officers to share with one another which approaches worked and which ones didn't. Learning from each other can not only reinforce goal ownership, but also minimize insufficiencies while striving for these goals.

Additionally, be sure to gather feedback to better refine strategies and the execution process regularly. Having a feedback mechanism allows management to fine-tune the process, while bank-wide strategies continue improving from a top-down and also a bottom-up approach.

Management can create great strategic plans, but regular customer interactions come from the front lines. Make sure strategies developed on high are executed as expected by the front lines by clearly communicating the goals, achieving goals, tracking and measuring with the right tools and providing pathways for peer review and feedback. In this way, everyone is committed to the same goals and expected results, and that is good for business.

For more information on developing strategies and executing for profitability, contact Earl Charneske at (847) 531-0890 or echarneske@pcbb.com.