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THE HUNT for revenue

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The hunt for revenue

Bankers seek—and find—new ways to pull up sagging revenues in a tough environment

By Melanie Scarborough, contributing editor

The old adage, “If you have money, you can make money,” no longer holds true for banking. Battling hostile economic and regulatory forces, many banks are awash with deposits that too few customers can qualify to borrow. With interest rates in the basement, investment returns are nil. New laws and regulations cap the amount many banks can charge retailers for interchange and place restrictions on overdrafts.

Yet simply raising existing prices to fully recoup lost revenue is unten-

able. Novantas, a New York-based financial advisory firm, points out that offsetting the \$50 billion shortfall facing the industry this year would require a 1,500% increase in account-maintenance charges.

To boost earnings, banks will have to find new sources of revenue. To thrive, they will have to be creative. While many say they have not made changes yet, almost all are considering doing so—from charging for services they now offer for free, to repricing their products, to moving into new areas such as

insurance brokerage, or expanding operations like wealth management.

Bank of America caught the public’s attention when it announced a \$5 monthly fee for debit-card purchases. A handful of other large banks followed, including SunTrust and Wells Fargo. But in the face of very public hostility toward the fees, one by one all these banks announced plans to forgo the fee. So that particular source of new revenue is off the table for now.

The most prevalent change so far in the wake of the Dodd-Frank Act



is the elimination of free checking. A recent ABA survey found that only 45% of non-interest checking accounts now are free, down from 64% last year and 76% two years ago. Where it exists, free checking often carries conditions like those set by Bank of the Rockies, a \$328 million-asset institution in Grand Junction, Colo., which provides free checking to holders of newly named Summit Accounts—those with an average monthly balance of at least \$1,000. Accounts that maintain a lower average are assessed a charge of \$8.95 per month.

Customers at Bank of the Rockies also can qualify for free checking by making the shift from paper to electronic statements—a requirement that proved unpopular among some low-balance customers who don't have computers. Those who contacted the bank were given an extra month or two to find an alternative, but continuing to accommodate them long-term isn't feasible, says president and CEO Peter Waller. "While we're sympathetic to their circumstances, we just can't continue to provide low-balance customers with free paper statements," he says, "not while the government is taking so much fee opportunity away from the industry."

Give fees a chance

To help recover lost revenue, there should be a charge to get a paper statement, agrees Randy Roth, CEO of Vitex Inc., a bank consulting company headquartered in Mooresville, N.C. He is flabbergasted by the number of banks that continue to bear the cost of printing and mailing statements. Customers who insist on receiving paper statements should be charged for that preference, Roth says, while cautioning that such changes have to be made carefully to avoid being cast as "the big, ugly bank down the street."

Roth advises a revenue-enhancement process that begins with a bank looking at each product and service it offers and considering adjusting the price. To be sure that you help your business rather than hurt it, know what your competitors are doing; know national prices; know what your local market will bear. "Then develop a strategy for slowly starting to ratchet up pricing over time," says Roth.

As another consultant observed about deposit interest rates in an article last month, competitors often will follow the change after someone makes the first move. It

could be similar with service charges. (See “The search for earnings,” p. 18, Sept. *ABAJ* digital edition on abaj.com.)

To avoid alienating customers, simultaneously explain the reasons behind higher fees. “You have to let customers know that the government has mandated changes and we have to charge for things we didn’t used to charge for,” says Roth. “If banks do a good job [explaining] that, most people will understand.”

Sometimes it isn’t the fee itself but the way it’s presented that makes it objectionable, says Mike Moebs, founder of Moebs Services, an economic research company in Lake Bluff, Ill. Overdraft protection,

for instance, is a service customers don’t mind paying for if they view it as a safety net. Resentment boils only when the fee is perceived as a penalty.

“More people voted to say they want overdraft protection than voted in the last election,” quips Moebs, and smart banks will profit from consumers’ preference.

Lower what you charge for overdrafts, he advises, and bank revenue will go up. The reason? If the payday lender charges \$17 for an overdraft, and the bank charges \$28, the bank isn’t an appealing option for customers who keep thin margins. But lower the overdraft charge to less than \$20—a psychological threshold—and the bank becomes competitive.

“Your own customers will decide that overdraft protection is now a

reasonable safety net and stay with the bank, so volume will increase,” says Moebs. “The second increase is that people will move away from payday lenders, as well as megabanks that are charging \$34 for an overdraft. Everybody wins.”

Banks must keep in mind, however, that fee income isn’t a stable revenue source because customers ultimately will find a way to avoid it, says David Albertazzi, senior analyst at Boston-based Aite Group. “If they’re going to be charged to use their debit cards, they’ll switch to cash or credit,” he says. “If I’m charged a fee unless I keep a certain account balance and deposits, then I’ll be sure to meet those minimums. If I’m using paper statements, the day the bank charges me

for that, I’ll say it’s time to move to electronic.”

Customers can also change banks, of course. Recognizing that, Albertazzi says imposing fees perceived as punitive is particularly risky for large banks because they can drive customers to small banks and credit unions, which typically are less reliant on noninterest income.

Rethink “free” and “waived”

Banks have only themselves to blame for *some* lost revenue, says Mike Moebs. He urges them to look at the services they provide free of charge and stop giving away what they could sell. For example, why not charge \$5 to \$10 for a cashier’s check? That’s a high-risk transac-

tion that has to be done correctly, he says. There’s no reason it should be free.

And why not make money for notarizing, a service many banks give away? When Moebs needed documents notarized recently, he went to the UPS Store, which charged by the page. The total came to \$64 (fees vary by state regs), which could just as easily have been earned by his bank. “Every bank has at least one notary,” Moebs says. “Charge for it.”

Fidelity Bank, Dearborn, Mich., recently had a task force look at the bank’s fee structure. “Guess what we found out? We were giving away a lot of stuff for free,” says Michael Ross, president and CEO of the \$900 million-asset bank.

One change Fidelity made was to begin charging customers

for loan extensions. When it was time for one customer to renew his loan recently, and he said he needed a few months to gather his tax returns, the bank put an end to offering its time for free and began to charge for that waiting period.

“We’re reconfirming all of the things we do and provide for our customers and making sure that where we should be compensated for service, we’re getting properly compensated,” says Ross.

Fidelity also examined the fees it was waiving and realized that, like many banks,

it was forfeiting a lot of revenue. To prevent that loss, Roth advises banks to adopt a policy that if someone waives a fee, they must report that in an email to the bank's president. "All of a sudden, your bank waivers go to zero," he says. "Sometimes the simplest things are the easiest."

Go high-tech

Other tactics require more specialized skill. Fidelity employs Vitex to look at all the bank's accounts payable for revenues that might have slipped through the cracks—e.g., an invoice that was paid twice,

unclaimed credit with a vendor—as well as to negotiate contracts so the bank buys only what it needs and pays only what it must.

Randy Roth also reminds clients that "there's a huge opportunity in the mortgage business because the mortgage broker is almost extinct at this point." But because the interest rates that drive mortgage demand fluctuate, it is difficult for community banks to maintain adequate staff during feast and famine. Consultants can help design systems where the bank's human resources shift with the market without having to hire and fire, says Roth.

Moreover, technology can alert banks to when a customer becomes an unexpected source of revenue. For example, if a client sells an asset and suddenly has half a million dollars cash sitting in his account, there should be a trigger to alert the bank of a new opportunity to suggest options, says Omer Sohail, director of Deloitte Consulting LLP. "A financial adviser should call that guy within 48 hours to talk about investments," he says, "but that doesn't happen much."

Enhanced data can boost revenue by creating better risk profiles. Sohail points out that when an individual pays off a credit card balance, the bank is likely to lower his risk profile—perhaps unaware that the customer took out a home equity loan to pay that bill. Putting together all that data is "absolutely possible," Sohail says, enabling banks to target better customers.

Break into new business

Additionally, banks can grow their revenues by expanding products

and services they already offer and by moving into new ones. Moebs advises banks to "look under your nose for the things you might have expertise in." Quite often banks have someone on staff who's an expert in retirement-account management, he says—someone who has kept up with regulation and attended seminars on IRA and Keogh accounts. If the bank is not utilizing that person's knowledge, it is missing out on a growing revenue stream: Baby boomers are projected to be the most attractive retail profit source until 2020.

According to Deloitte Consulting research, "As boomers age and adjust to the lingering realities of the financial crisis, their financial behaviors are shifting from an emphasis on short-term consumption to protecting their long-term security through saving, insurance, investment, and retirement income products." Their vast numbers make that demographic a prime source of revenue for banks.

Insurance brokerage is another area proving profitable for banks willing to depart from traditional offerings. Although about two-thirds of banks make some income from insurance brokerage, fewer than 20% report that it's a significant component of their earnings. Yet the potential clearly is there. According to the *Michael White—Prudential Bank Insurance Fee Income Report*, banks generated a record-high level of insurance brokerage income in the first quarter.

A particularly appealing aspect of the insurance brokerage business is that it is a low-risk enterprise: Carriers, not brokers, bear underwriting exposure for the insurance they sell. Moving into insurance brokerage also isn't capital-intensive. Banks can onboard the operation without outlays for new branches or equip-



ment. (See “Insurance Revival,” p. 40 in Sept. *ABAJ* digital edition, on abaj.com)

Yet despite the potential revenue, many banks seem reluctant to branch out. In fact, Roth observes them doing just the opposite. “They might have an insurance organization, but it was only marginally profitable so they’re divesting,” he says. “They’ve decided, ‘We’re going to do what we do, but do it really well and really efficiently.’”

The point can be argued round or flat; much depends on circumstances.

Fidelity Bank, for one, adheres to the philosophy that they’re better off sticking with what they know. Already offering a broad range of products and services to seemingly satisfied customers, it has no impetus to expand offerings, says CEO Michael Ross. Because the bank’s market in southeast Michigan was hit hard by the downturn in the automotive industry, his bigger concern is dealing with the “significant number of customers having a hard time paying right now.”

Make regulation pay

While no one pretends that Dodd-Frank doesn’t hamper revenue, some of the fine points of the law can be turned to banks’ advantage. For example, Dodd-Frank eliminated the ban on paying interest on commercial checking accounts, creating an opportunity that Moebs is surprised more banks haven’t seized.

He points out that there are 27 million small businesses in the United States—many of which operate on tight margins and could benefit from their bank providing detailed invoicing and account analysis. If banks offered those services

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where we should be compensated for service, we are”

— Michael Ross, Fidelity Bank

for additional charges, along with interest on commercial accounts, the interest paid would be offset by the additional revenue. “Walk into a new prospect and say, ‘Is your bank sending you these analyses? We will.’” Moebs suggests. “This is a grand opportunity to take the death of Reg Q and convert it into profit on business accounts.”

A bright spot in the cards

One product area untouched by Dodd-Frank has some banks seeing black. While new rules cap fees for debit card transactions, Congress did not address charges related to prepaid cards. Now that almost half of all Americans receive some form of government assistance, a particularly good prospect is the business of issuing electronic benefits cards.

Banks in the vanguard include JPMorgan Chase, which provides cards for Michigan’s unemployment insurance program. Targeting this market means previously unbanked customers now may be a valuable source of revenue. But prepaid cards overall can be a significant new revenue source.

Business Solutions, a subsidiary

of ABA, offers a turnkey, bank-branded, prepaid solution for ABA members. Bank customers use prepaid cards to pay employees, support college students, or help people using alternatives to traditional checking accounts.

“Regardless of size, banks see the landscape for payment cards is changing,” says Bill Kroll, president of Business Solutions. “Many people already use prepaid cards as a safe, convenient alternative to cash, and the financial institutions offering these cards are seeing explosive growth.”

If banks increased by only 15% the amount of business done by each customer, that would offset the \$50 billion revenue shortfall, according to Novantas. That has bankers considering onboarding customers they would not have approached a few years ago.

“It’s not banking as usual at all,” says Roth. “Banks are really being pressured for earnings, and good bankers are looking at all areas of the bank to find profits. The ones who are going to stay around have realized that the entire world has changed, and they have to think differently.” ■