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THE ART OF BANK PLANNING
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The Relationship Between Problem Occurrence and Customer Satisfaction

Part 2 of 2

In the May 2004 issue of Bancology (Volume 11), the severe negative impact of perceived bank created problems or errors on customer satisfaction and loyalty was illustrated. Most problems or errors are not the result of blatant errors by the institution; however, if the customers perceive them as such, the fault still lies with the bank for not better explaining account features, fees, policies, procedures or simply showing empathy. This article will explore these perceived problems in detail and suggest how to curtail their occurrence.

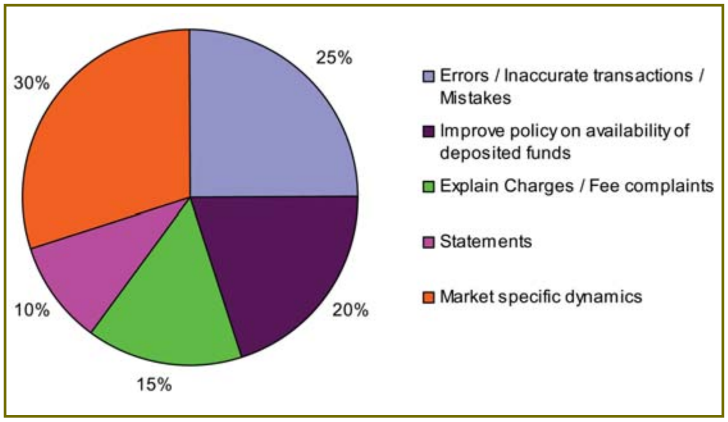
No matter the size of the institution or the market in which it competes, the major descriptions of the problem that occurred fall into the following groupings:

1. **Customer service / errors / inaccurate transactions / mistakes**
   Mistakes by branch or back office personnel are the culprit for approximately one quarter of the experienced problems or errors cited by customers. These are usually careless errors that have been remedied by the bank, like misspelling some of the customer's information, the debit card that never arrives, etc. Although these are not grave issues, customer satisfaction and loyalty are deeply affected.
   Remedy: Continuous training of employees, especially those on the front line.

2. **Availability of deposited funds**
   About one fifth of the reported problems are due to the availability of funds policy. Although the institution has technically done nothing wrong, customers do not understand this policy, thus leading to overdraft fees, etc. Usually, these customers are informed of the policy when they are in the branch trying to reconcile the issue.
   Remedy: Explain this policy and others during the account opening process.

3. **Explain charges / fee complaints**
   Customers are the most frustrated when they discover a hidden fee or a breach in a policy that they did not know existed.

continued on page 2



Inside the Wallet of the American Household

Both consumers and bankers often perceive banks as the primary custodian of consumer assets. When consumers consider their own financial situation, they will typically think in terms of immediate liquid assets – those deposits held at FDIC insured depository institutions. However, bank deposits represent only a small portion of consumer assets.

The Federal Reserve Board's Flow of Funds Accounts, released quarterly, reveal a much deeper portrait of the holdings of US households. American households own a collective $53 trillion worth of assets, and bank deposit accounts comprise only 10% of this total. In fact, much of the nation's assets are non-financial, and even a significant portion of the financial assets are highly illiquid.

Real estate represents 28% of all household assets, and consumer durable goods (furnishings, appliances, automobiles…) account for another 6%, so approximately one in three consumer dollars are invested in tangible rather than financial assets. Among financial assets, 18% are held in pension funds, representing an opportunity for banks in institutional asset management, and 11% are bound in the value of owned businesses, representing an opportunity for business bankers.

But the value of these illiquid financial assets – some $15 trillion in all – still represents a long term opportunity for consumer bankers too. As employees retire, pension balances will be disbursed and liquidated; similarly, business owners will retire and sell their equity positions in their businesses. Bankers that probe consumer needs from the outset of the banking relationship will be aware of, and presumably well positioned, to capture such assets as they turn liquid.

continued on page 2

THE ART OF BANK PLANNING

continued from page 1

The Relationship Between Problem Occurrence and Customer Satisfaction

Even though the bank employee explains the reason for the fee to the customer when he calls or visits the branch, agitation and distrust have already damaged this relationship.
Remedy: Explain this policy and others during the account opening process.

4. **Statements**
Some type of problem with the statement contributes to about one tenth of the errors experienced by customers. These complaints vary from not receiving the statement one month to an error that requires the customer to make an extra trip to the branch for resolution.
Remedy: Simplify the statement for ease of understanding. Also improve quality control of the data source contributors.

5. **Market specific dynamics**
The previous four types of problems account for about 70% of all perceived bank created errors. The remainder of the problems that occur is unique to the institution and the market. The competitive complexion of the market influences the consumers' financial comfort, thus their expectations. For example, in large metros where convenience is the dominant reason for selecting the institution, an outdated network will fuel many complaints. In a smaller market, employee turnover and banking hours will create problems.
Remedy: Know and understand your institution and competitor's weaknesses. Further, management must understand consumers' financial behavior in the various markets within its footprint.

Inside the Wallet of the American Household

continued from page 1

Nearly every bank has added some capabilities in investment and insurance sales in an effort to capture a greater share of the consumer wallet, and the Flow of Funds tables justify these efforts. American households own over $12 trillion in securities and insurance assets, or nearly 2.5 dollars for every dollar held in traditional bank deposits. These assets may be held in bonds, stocks, mutual funds, annuities, or other instruments, but only a small proportion are purchased through banks. Interestingly, despite the banking industry's investments in the securities sales channel, the erosion in stock values over the past several years has fueled a flight back to traditional bank instruments. Although bank deposits comprise a similar proportion of assets as in 2000 (10% vs. 9%), deposits comprise 16% of financial assets, up from 13% in 2000.

Real estate has shown the greatest gains of any consumer asset since 2000, as the value of owned real estate increased by 35% and now represents 28% of all consumer assets. However, mortgage debt has grown at an even faster pace. Mortgage balances of all types (first mortgages, home equity loans, home equity lines of credit) now equal 13% of household assets, up from 10% in 2000. Similarly, total consumer debt as a function of assets has also increased, from 15% in 2000 to 17% today. The inevitable consequence of mortgage borrowing outpacing real estate values is a decline in equity; owners' equity now represents only 54% of home values, down from 57% in 2000.

Installment and revolving credit show a similar trend to mortgages; while such loans account for the same share of total assets as in 2000, the two categories represent 15% of liquid assets (deposits and securities), compared to 13% in 2000. Bankers must judicially monitor consumer debt ratios in order to maintain credit quality standards. The increase in real estate values has masked a significant amount of consumer borrowing, and any downturn in real estate values could constrain the ability of households to support current debt levels.

The above statistics reveal both opportunities and warnings to bankers. Both the Federal Reserve and the FDIC publish numerous studies on trends in household investing and borrowing (see Bancology February 2004 issue [Volume 10] for more on publicly available information sources), and bankers can gain valuable insights by monitoring these trends.

Product Note

THE ART OF BANK PLANNING
bancography PLAN
Market Analysis and Branch Planning Software

We are pleased to announce the latest release of *Bancography Plan*, our innovative branch planning software tool. This newest release includes three valuable enhancements:

- Our branch database now includes all credit union branches, not just the main offices.
- The branch database also includes all branches opened as of June 30, 2004 – even those opened since the most recent FDIC reporting period, June 30, 2003. We are now pursuing quarterly updates to the branch table through online downloads.
- Users can now enjoy much greater control over the branch map, including the ability to suppress branch labels and/or branch markers and to omit specific branches entirely as needed.

If you're not already using *Bancography Plan*, call 205.252.6671 to receive a demonstration CD or visit www.bancography.com.

How to Analyze Branch Demographics

Market demographic information can provide tremendous insight when considering whether to deploy a new bank branch. While every branch analyst uses a preferred set of demographics, Bancography contends that certain statistics merit configuration in any new branch review.

Households: The absolute number of households provides the simplest benchmark of market size. Because financial purchase decisions are typically made at the household rather than the individual level, household count provides a more useful measure than population count. On average, mature bank branches carry at least 2,000 – 2,500 households, so a branch trade area should offer at least that many households, and considerably more if the area includes numerous competitors.

Growth: Usually stated in percentage terms as a five-year forward estimate of household growth, this identifies the degree to which the market size will increase during the branch's initial growth phase. Be sure to always convert growth percentages to absolute household counts; a 20% five year growth rate on a market of only 1,000 households equates to just 40 new households per year. As a basis for comparison, the five-year projected growth rate across the entire US is 6.2%.

Turnover: While household growth refers to the change in the number of households, turnover also involves new residents in a market, but counts those moving into existing housing stock. A market may have 1,000 households today, and no projected growth and thus 1,000 households five years from now. But if the market's five-year turnover is 30%, it indicates that 300 of the 1,000 households will have new occupants within five years. Turnover creates opportunity for banks because new residents, faced with different commuting and shopping patterns, are more likely to consider changing banking providers.

Density: Calculated as population per square mile, density is helpful in determining the extent of a branch's trade area. The higher the density, the smaller the trade area. In dense urban areas, density may exceed 15,000 residents per square mile, indicating trade areas of less than one mile. In rural areas, density may fall below 500 residents per square mile, indicating a drawing area of up to five miles.

Median age, head of household: The age distribution of a market reveals information about the product demand. Median age can be stated as a population median age or median age of the head of household. Because the former measure includes children, it skews the median downward and yields a value that does not accurately describe the financial decision makers in the market. The head of household measure is a more representative statistic. The US median is 47.4. This statistic rarely falls below 40, but in retirement markets can exceed 70.

Percent of households with children: Highly correlated with median age, this statistic helps frame the composition of the market in terms of the prevalence of families. Across the US, 34% of households have children present. Markets with a significantly higher proportion of households with children will show higher borrowing needs and higher transaction activity.

Median household income: Average balance levels of nearly every product increase with income, so this statistic offers a strong proxy for financial product demand. Household level income is useful because most financial decisions occur at the household level; per capita income is less useful, as it is diluted by the presence of children. Medians are preferable to averages because extremely high income outliers will skew averages upward, leaving a distorted view of the typical market household. The median income for all US households is $43,700.

Percentage homeowners: This statistic offers an immediate indicator of potential for mortgages and home equity lending products or potential for commercial real estate financing for multifamily residences. 67% of American households own their homes, and 33% rent their homes.

Median home value: Typically reported from Census Bureau or local assessment data, this measure proves most useful in gauging affluence in retiree markets where income remains low even though asset levels may be high. In non-retiree markets, home values stay highly correlated with income. Use this statistic with caution and as a relative measure only, as the methods by which median home value is calculated often yield values below actual available purchase prices. The median US home value is $116,000.

Businesses and employment: The number of businesses reveals demand for business checking and lending products, while the number of employees shows the extent to which a market's daytime population exceeds its residential population base. Examine the composition of the market's employment; a high proportion of manufacturing jobs indicates a higher wage base, and thus higher deposit potential, than a market dominated by service sector and retail employment. Dividing employment by population yields a useful ratio for comparing markets. If this statistic exceeds 1.00, the market can be considered high employment; in typical suburbs the ratio runs at about 0.70. Values below 0.35 indicate residential only markets; be sure that branches in such markets are configured exclusively for consumer demand.

Both Kimberly Clay and Steven Reider will teach at the **ABA Marketing Conference** this September. In the *Branch Development* session, Steven will present the fundamentals of branch planning, including market level network planning, evaluation of new branch opportunities, site selection and branch closure decisions. In the *Creative Marketing Research* session, Kimberly will present how to design and execute research projects with little or no budget and share case studies, samples and syndicated research. For more information, visit *www.aba.com*.

Bancography will participate in the following conferences this fall:

- **American Bankers Association Marketing Conference**
  September 12-14, 2004, Scottsdale, Arizona
  For more information, visit *www.aba.com*
- **BAI's Retail Delivery Conference & Expo**
  November 16-19, 2004, Las Vegas, Nevada
  For more information, visit *www.bai.org/retaildelivery/*

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