VOL. 21

December 2006

BANCOLOGY
a quarterly journal

THE ART OF BANK PLANNING
bancography

THE ART OF BANK PLANNING

What to Score on a Branch Scorecard

With institutions nationwide incurring high costs for new branches, facing increasing competition, and anticipating impending margin compression, there is a greater premium than ever on maximizing branch sales. Accordingly, many institutions are implementing or refining their branch incentive programs. But the success of any incentive program depends directly on the measures against which participants are evaluated. Although every bank or credit union should tailor its scorecard to its specific strategic objectives, several factors should remain constant to any scorecard. Bancography's recommendations for structuring a branch scorecard follow.

The primary goals of a performance scorecard are to reinforce the behaviors taught in sales training classes, and to reward super-normal performance. Thus, the scorecard should track the major activities that occur in daily sales interactions, and should pay incentives only for volume levels that well exceed what otherwise falls under the category of 'doing our job'.

For a scorecard to succeed, the branch staff must easily understand how they are being scored and compensated. Therefore, keep the number of categories manageable, to no more than the six or eight most important sales and service behaviors. Set goals that are aggressive but attainable. Aggressive goals insure that payouts only occur for superior performance; but if goals are overly aggressive and perceived as entirely unattainable, it will discourage all sales activity. And pay frequently enough – either monthly or quarterly – that branch staff see a direct link between their daily activities and their rewards for such activities.

The scorecard should include only measures directly controllable by the branch staff. For CSRs and tellers, consider scoring in terms of units sold rather than dollars added or profit contributed. By focusing on units (for example, number of checking accounts opened), the scorecard removes any bias against needs-based selling. The scorecard encourages CSRs to offer whatever product best fits the consumer's need, regardless of the product's profitability. Profitability should remain the province of corporate product management, and CSRs should sell whatever the customer needs, secure in the knowledge that the company has priced the product appropriately to insure profitability. Further, CSRs have little control over what balances a customer brings, but much more control over what products they present to the customer.

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Findings from the 2006 FDIC Deposit Statistics

In late October the FDIC released its most recent branch level summary of deposits. The data, compiled each year as of June 30, represent the only branch-level deposit statistics for banks and thrifts available across all institutions nationwide. When combined with the NCUA's quarterly reports, the data give a comprehensive view of branch banking trends in the United States.

US financial institutions added almost 3,000 net branches last year, and there are now over 112,000 branches across the country. Note that the net increase reflects the difference between new openings and branch closings, so the actual number of branches constructed exceeds 3,000. Six states saw net gains of over 100 branches, led by Texas with an increase of over 400 branches. These six states (Texas, California, Florida, New York, Illinois, and Georgia) accounted for over half of all branch growth nationwide.

Over the past five years, the Chicago metro has led the nation in branch growth, often accounting for as much as 25% of all branching activity nationwide. But this year Chicago ranked third, behind New York and Dallas which added 225 and 175 branches, respectively. Chicago still added over 150 branches, and Los Angeles over 100; other leading metros included Houston, Miami, Atlanta, Washington DC, Phoenix, and St. Louis.

The nation's deposit base increased by 8.3% between June 2005 and June 2006 to reach almost $7 trillion. That pace matches the growth rate from June 2004 to June 2005, and slightly exceeds the 7.5% average annual growth rate of the last ten years. The share of deposits held by credit unions declined slightly to 8.7%, the fourth consecutive decline in that statistic after reaching a peak of 9.4% in 2002.

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How to Choose the Proper Data Collection Vehicle

There is no right or wrong method of data collection as long as the client understands what will be delivered and/or the limits of the data collected. For instance, if an institution requires statistically-valid data in order to build strategies, incentives and policies, then that institution should implement a telephone-based methodology. If an institution wants to explore broad behavioral or exploratory topics, then it may utilize focus groups or mail-based studies.

- **Telephone interviewing** is the best overall method for gathering data, because it allows one-on-one contact with the customer. Due to the integrity of the data garnered from telephone interviewing, results can be used to affect incentives, strategies and in extreme circumstances, employment termination. Statistical significance and cost move in lock-step, so telephone interviewing is usually more expensive.
- Although there are about twelve people in a **focus group**, the opinion is the consensus of that twelve as a collective whole, not individual opinions. For this reason, it is qualitative research and not statistically significant. When exploring an issue such as a possible new product offering, wording or phrasing that would be clearly understood by customers or developing hypotheses and surveys for larger studies, focus groups are the best method for gathering data.
- An institution utilizes **mystery shopping** to observe behaviors necessary for sales and service. Mystery shopping is the view of a single individual who is neither a customer nor an employee of the institution. Therefore, mystery shopping does not measure customer satisfaction, because a customer does not supply the information. Information gathered from mystery shopping is subjective and should be used for coaching employees and improving training.
- **Mail-based studies** are best used when the institution needs to measure customer satisfaction, new loans, new accounts or new mortgage customers, yet budgetary constraints will not allow telephone surveying. The drawback to mail is that there is no guarantee that the actual customer is the one who completes and mails in the survey. Another negative to mail is the response rate, which is usually below 8%. Typically those who respond fall into the extreme categories: very satisfied or very dissatisfied. Mail is adequate for changing direction within an institution and employee bonuses, but not for finite change.
- **Comment cards** in the branch or statement stuffers are excellent compliments to a service quality program but are weak as sole providers of information. Both of these data collection methods serve as effective public relations tools, for they communicate how important the customers' opinions are to the institution. Although it is healthy for customers to freely express their opinions, as with any non-controlled respondent methodology, there is no proof of who actually completes the survey. Responses also tend to be extreme: very satisfied or very dissatisfied.

Regardless of the data collection methodology chosen, the data gathered is only as good as the sample provided by the institution. For instance, if the sample provided for telephone surveying only contains one correct phone number for every twenty names, the calling sample will only represent 5% of the population. Bancography's interviewers average a 25% response rate for retail and 22% for businesses. Therefore for this example, the data gathered would only represent 1.25% of the client's population (5% sample x 25% response rate = 1.25%).

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Branch manager scorecards can include profitability measures that reward efficient operation of the office, but restrict these measures to controllable elements too. A branch manager has little control over lease payments or utility bills. Further, if scoring on expense control, use care to insure that long-term retention is not compromised by branch managers reducing staff to meet short-term expense targets.

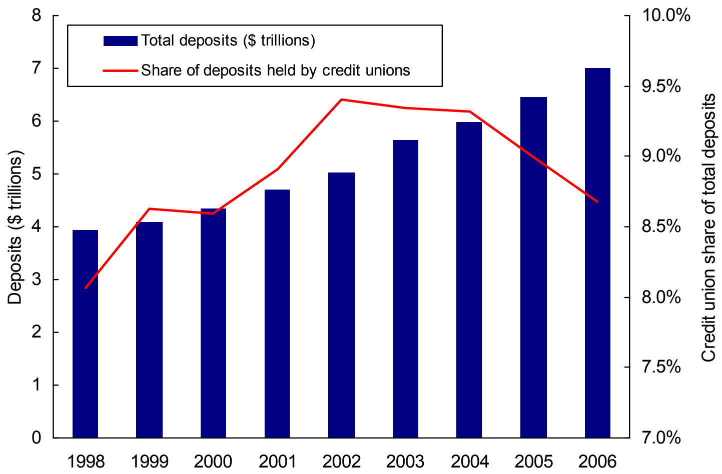
Do not include sales of CDs on the scorecard. CD sales are largely rate-driven and balances will be greatly affected by decisions of the asset liability committee well beyond the control of branch staff.

Include some measurement of service quality or retention in order to discourage behaviors that foster high account turnover. Including a retention measure encourages needs assessment at the point of sale and follow-up service calls after the sale.

Offer incentives for referrals to other departments. Because referral opportunities to mortgage, investment, insurance, and other departments are less frequent events, CSRs may otherwise overlook these customer needs.

Negate payouts for basic failures. No level of sales volume can offset poor administrative oversight, and insufficient audit results, excessive over/short situations, and low service quality scores should all override any sales performance level.

Findings from the 2006 FDIC deposit statistics



The list of leading deposit gaining states reflects regulatory and environmental issues. Deposits in South Dakota and Nevada increased by over 75% during the past year, and Utah's base increased by over 20%. These gains were impounded in industrial loan corporations and credit card banks, which face favorable regulatory environments in those states. Louisiana and Mississippi ranked third and fifth with deposit gains of 25% and 21%, respectively, and these gains represent a return of post-Katrina funds, boosted by significant insurance settlement funds that remain undisbursed pending construction and permitting issues.

Beyond those states, New York posted an increase in deposits of 15% over the past reporting year, and eight other states (Georgia, Texas, Idaho, Delaware, Wyoming, South Carolina, Pennsylvania, and Virginia) showed gains of at least 10%. While the Delaware gain impounds substantial deposits held by credit card banks and the Wyoming and Idaho gains occurred on the smallest and sixth-smallest bases in the nation, the other gains represent substantial absolute as well as relative growth.

To learn about deposit trends in your market, visit the FDIC Summary of Deposits web page at *http://www2.fdic.gov/sod/index.asp* and the NCUA Quarterly Information web page at *http://www.ncua.gov/data/FOIA/foia.html*, or call Bancography for additional information about your market area.

An Uncertain Future for Industrial Loan Corporations

A recent application for deposit insurance filed by Wal-Mart Stores, Inc. has caused widespread speculation as to the intentions of the retail chain and furthered the debate on keeping banking and commerce separate. Other major retailers such as Home Depot have also filed deposit insurance applications. Is this a sign of a developing trend? And if so, what is the threat behind the notion of major corporations entering into the banking industry?

The early 1900s ushered in an era in which Industrial Loan Corporations (ILCs) were created by major manufacturing firms to help blue-collar workers obtain credit and satisfy their need for financial services. The FDIC defines ILCs as institutions owned by commercial firms that are not regulated by a federal banking agency. Although ILCs offer many of the same products and services as other commercial banks, they are regulated differently than banks. For example, ILCs may not accept demand deposits and the parent companies of ILCs – unlike bank holding companies – are not subjected to federal supervision on a consolidated basis.

Historically, ILCs have not received much attention as a threat to commercial banks but perhaps it is Wal-Mart's ability to target the "underbanked consumer" that sparks fears that ILCs could dilute the pool of potential bank customers. There is a growing population of consumers who need basic financial services but do not use commercial banks for all of their traditional banking needs. A recent study conducted by American Banker surveyed the banking habits of low- and moderate-income neighborhoods in three cities. The research indicated that 26% of banked households still use non-bank providers to cash their checks and 38% paid their rent with money orders or cash.

Whether or not this is an indicator of future pursuits by ILCs remains uncertain. However, since the Wal-Mart application was filed, the FDIC has placed a six-month moratorium on all ILC applications. The FDIC states it is using this period to evaluate the risks that any new applications may pose to the insurance fund and whether or not exceptions will be granted. In July 2006 Congressmen Paul Gillmor (R-OH) and Barney Frank (D-MA) introduced the Industrial Bank Holding Company Act of 2006, which would change current banking laws and prohibit new commercial firms from acquiring industrial loan companies, as well as limit interstate branching by ILCs. However, the bill was not passed before the adjournment of the 109th Congress.

Wal-Mart currently maintains alliances with numerous financial services providers. Institutions as diverse as SunTrust, Woodforest National Bank, and Tropical

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An Uncertain Future for Industrial Loan Corporations

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Financial Credit Union maintain branches in over 1,000 Wal-Mart stores, which would appear to preclude deployment of a Wal-Mart owned bank. But Wal-Mart operates over 3,500 stores in its various formats (Wal-Mart, Supercenter, Sam's Club, Neighborhood Market), leaving ample room for expansion if it pursued its own retail branch network. Wal-Mart executives continually deny that its application to the FDIC is a forerunner to establishing a retail bank, but the precedent that approval could grant would allow companies such as Target and Home Depot, each of which operate nearly 2,000 stores nationwide, to build retail banks even if Wal-Mart used its charter solely to gain efficiencies in transaction processing.

The FDIC's decision must ultimately reflect that organization's primary responsibility – the safety and soundness of the American banking system. To the extent that ILCs could allow co-mingling of the banking and corporate sides of a company in a manner that threatened the institution's liquidity, the FDIC would need to seek expanded powers to regulate the parent company too before granting the tacit endorsement of the subsidiary bank that deposit insurance would provide. But if corporations are willing to cede to the FDIC and other supervisory agencies the same access that those agencies currently have to bank holding companies, then the specter of increased competition offers a tenuous platform on which to predicate arguments against expansion of ILC branch networks.

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