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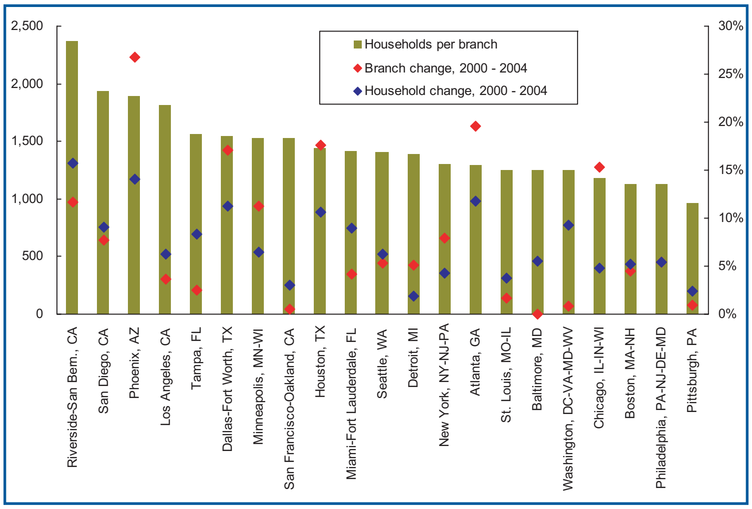
Branch Concentration: Some Markets Increasing; Many Unchanged

In a previous Bancology article two years ago, we discussed the concentration of bank branches in the nation's largest metropolitan areas. With the release of the FDIC's June 2004 deposit statistics, it is timely to revisit that topic.

There are 21 metropolitan areas in the United States with over one million households. These metros contain nearly 40% of the nation's households, and nearly one-third of the nation's bank branches. The metros have seen diverse growth in branches and households over the past four years. The northeast remains the most concentrated branch environment, with five of the six most concentrated branch markets sitting between Washington DC and Boston. In contrast, the six least concentrated branch markets all sit in warm weather locales, including three in southern California.



Since 2000, seven metros have enjoyed double digit growth rates in branches, with Phoenix and Atlanta leading with 27% and 20% increases, respectively. The seven metros with double digit branch growth rates include the five metros with the highest household growth rates, but also Chicago and Minneapolis, two metros with low to moderate household growth.

In 9 of the 21 metros, the pace of branch growth outstripped the household growth rate, leading to increased branch concentration. Although branch growth and household growth show some relationship, the slowest growing metro, Detroit, with household growth since 2000 of only 1.9%, showed 5.1% branch growth in that same period. In contrast, Riverside – San Bernardino posted the highest household change, 15.7%, but observed only an 11.7% change in its number of branches.

Many industry periodicals and conference presentations have debated whether an apparent industry-wide increase in branching is leaving some markets overserved. In aggregate, branch concentration is increasing only slightly across the top metros, with much of the change occurring in a few markets that have seen numerous new entrants in recent years: Phoenix, Atlanta, Chicago, Houston, and Dallas. Across all the large markets, though, results are mixed, revealing little evidence that the pace of branching will decline anytime soon.

Using the ATM Network to Improve Retention

Several recent projects focusing on ATM expansion initiatives revealed a correlation between ATM network coverage and customer retention. The studies classified households by the proportion of transactions that they conducted on foreign versus on-us machines, and by whether the machine they used most frequently was a foreign or an on-us machine. In one study, the data revealed that in areas where foreign ATMs supplied over 25% of transactions, attrition was four percentage points greater over a six-month period than in areas where foreign ATMs supplied less than 25% of transactions. In another study, over a six-month period the attrition rate of customers whose most frequent ATM was a foreign machine exceeded the rate for the on us group by a wide margin, 7.9% for the foreign group vs. 6.4% for the on us group.

An underlying reason why the presence of ATMs is so broadly linked to retention lies in the way in which consumers use the ATM channel. Despite perceptions of the ATM channel as a remote, anytime, anywhere channel, the majority of ATM use, and especially on-us use, occurs close to the consumer's home. In one study, 50% of all transactions and nearly 60% of on-us transactions were conducted within three miles of the consumer's home. The median distance between a consumer's home and his most frequently used ATM was only 2.6 miles, and only 2.2 miles if his most frequently used ATM was an on-us machine.

In 48% of the households in the study group, the most frequently used ATM was the ATM that was the closest ATM to the consumer's residence of any of the ATMs used by that consumer during the past year.

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Using the ATM Network to Improve Retention

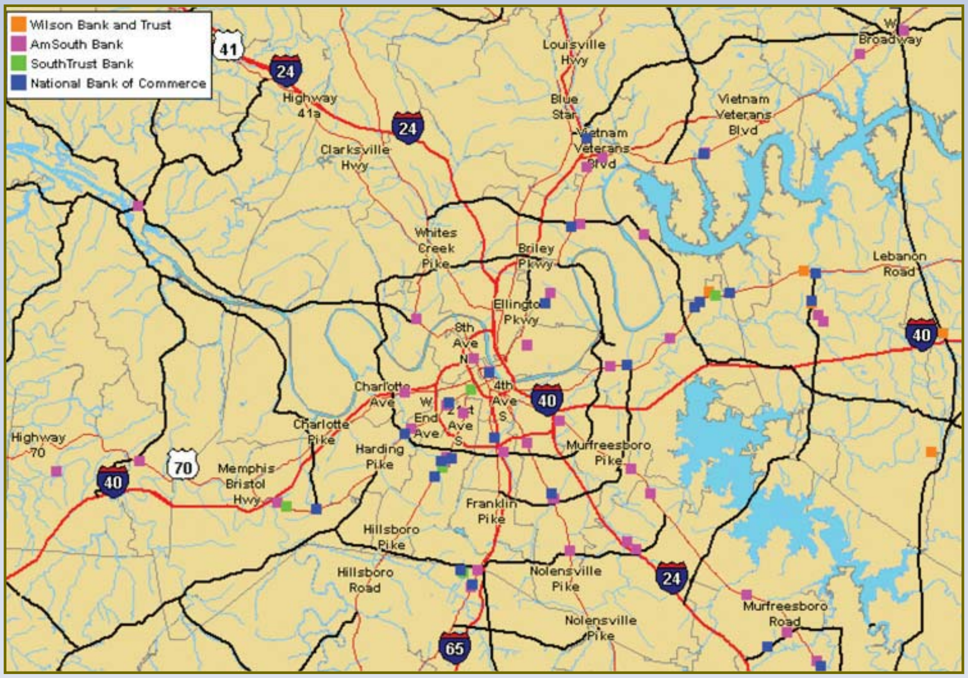
Additionally, the greater the distance between consumers and their nearest on-us ATM, the greater proportion of transactions the consumer ran at foreign ATMs.

With surcharges and foreign transaction fees increasing, consumers may now face fees of $3.00 - $4.00 for using foreign ATMs, after paying the surcharge to the terminal owner and the foreign transaction fee to their own bank. Thus, two or three foreign transactions per month can quickly eclipse the monthly fee paid for a typical checking account. Consumers who lack nearby alternatives for fee-free access will quickly find an economic incentive to shift relationships to institutions that can provide such access, even if doing so requires foregoing a no monthly fee checking account.

Surcharging has fueled an explosion in the number of ATMs available to consumers, but has also conditioned consumers to expect access to ATMs whenever needed. Yet by increasing the number of ATM transactions, and reducing the interval between ATM withdrawals, this phenomenon has also fostered more situations in which consumers may encounter fees, and thus more opportunities for consumers to evaluate whether their institution is providing the best economic value to them. If an institution can meet a consumer's need for cash with fee-free options a majority of the time, the consumer will reward that institution with continued loyalty. However, if a consumer routinely faces ATM withdrawal fees for accessing his own funds, he will quickly reconsider the viability of his current banking relationship.

Branch Site Identification: A Multiple Submarket Approach

When considering a new branch location, banks often evaluate a single location in an attempt to reach a yes/no decision. However, when entering a new market area, the bank may not have even identified a single target submarket. In this case, the bank needs a means of evaluating all potential submarkets in the target new market area.



Bancography assists banks in this process with our Branch Site Identification product. The first and most important step in the branch site identification process is the definition of submarkets. Bancography will identify all existing banking, retail, and commercial concentrations to define potential locations for evaluation. We will then forecast the likely drawing area for a branch at each location to define submarkets. Submarkets are defined in terms of census block groups, and are always exclusive, with no overlapping geographies belonging to more than one submarket. This insures that the sum of demand across all submarkets does not exceed the demand in the market overall.

After defining submarkets, we use the same models underlying our *Bancography Plan* software tool to forecast product demand in each submarket. We then evaluate the competitive environment to forecast market penetration and build a balance sheet and income statement for each submarket. This process yields a ranked list of the potential sites in the target market area, and helps the bank prioritize its initial market entry point and possible future network additions. All recommendations are supported with thematic maps showing key demographic statistics, competitor maps and assessments, and a discussion of the benefits and risks of each potential location.

Contact Laura Levie at 205.252.6671 for more information about Bancography's Branch Site Identification services.

How to Implement a Successful Research Project

This "How to Guide" is an excerpt from Bancography's Syndicated Research study, ***Marketing Research Benchmarks and Toolkit***. The following tips are based on helping the project manager focus on the marketing research directive. Bancography believes that preparation before writing the request for proposal or project plan will allow the process to run smoothly and guarantee that the end result will be successful.

Methodology: What do we want to know or measure? Once you have been assigned a topic for research, challenge the manager for more information, such as geographic boundaries, implications, pros and cons. Also find out from what management level this directive stems. Full understanding and comprehension of the objective will fuel focused time and energy.

Results: How will management use these results? Keep management focused on the objective and the ultimate need. Only ask those questions that are needed to complete the project. The longer the survey instrument, the more expensive it is. Also, a lengthy interview process may lead to customer complaints and termination of the interview.

When writing the survey, make sure that every question can be acted upon, or at least become a factor within a group of questions (indexes.) For example, consider a behavior that management has deemed part of the sales and service culture, like smiling at the customer. Independently, smiling has no correlation to loyalty; but, if it is a behavior that is important to the institution, it should be included as a service quality factor.

Frequency: How often do we track these measurements? Marketing research should be an ongoing commitment, not episodic. As long as the institution is too big to know every customer by name and invests in advertising, sales training, new branches and employees, it should conduct research.

It is important to those targeted by the research to see commitment by the institution. A monthly, semi-annual or even annual survey reflects a commitment to service quality and will increase the response rate, ultimately saving time and money. This is especially important for internal surveys. For example, if branch managers are surveyed on how the many departments within the corporation serve them, they expect some type of ongoing commitment before spending their time to complete a survey. This assurance demonstrates that upper management is involved and supportive of the research.

Sample size: At what level do the results need to be significant or actionable? The answer to this question will also determine the type of data collection, qualitative or quantitative. If this research endeavor is more exploratory in nature, then a qualitative approach is adequate, such as focus groups or one on one interviews. If the results are going to be used to change policy, set strategic objectives, or affect employee incentives, then a quantitative study is needed for the statistical significance.

Outsource versus in-house: How much staff, money and time can be devoted to this endeavor? The method of the data collection and the reason for choosing this method has many implications on whether the research can be conducted internally or externally. For example, a study that is politically motivated should be conducted externally. Any research that will affect employee incentives probably also should be outsourced. Basically, any research whose results are very sensitive and will affect careers should be outsourced.

However, any exploratory research on customer perceptions of service or products can be conducted internally. Research that can be conducted internally should be. Not only is money saved, but the corporate staff will learn volumes from customers. It is the project manager's responsibility to decide whether the objective can be met with internal resources and by whom. Once again, if the objective has political implications or ramifications, it is advisable to outsource the work to a third party.

Preliminary research
Once the objectives are clear, but before drafting the request for proposal or project plan, research the topic yourself. Conduct literature searches for white papers and other syndicated research on the Internet to become educated on this topic in the industry. Secondly, investigate this topic on the bank's competitors' web sites and those of financial industry leaders. Financial institutions, especially large players, are always posting news releases of their activities.

Preparing yourself on the research topic will enable you to answer questions from management. Further, costly primary research might not be necessary if secondary studies are available. Thirdly, if primary research is necessary, a targeted and cost effective study can be designed because you will be better able to direct your own external study.

Bancography's Steven Reider will present at the **Mid-States Banking Consortium** from March 23-25 in San Francisco. Representatives from 13 bank associations will attend this event.

Steven will also speak at **Synovus' ATM and Debit Conference** from March 7-8.

Steven Reider contributed to the American Banker Online article: ***"Design: A Retail Banking Concept that Has Stayed Hot,"*** published on January 18, 2005. Current American Banker subscribers may read the article at www.americanbanker.com.

Bancography is pleased to announce its membership in the **Credit Union Executives Society Financial Suppliers Forum**. For more information, visit www.cues.org.

Bancography will release a new syndicated study next month titled ***Attrition Benchmarks: Retail and Business***. This study will examine reasons for attrition from banks and credit unions and present benchmarks from over 20 participating institutions. For more information, contact us at 205.251.6227 or *research@bancography.com*.

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