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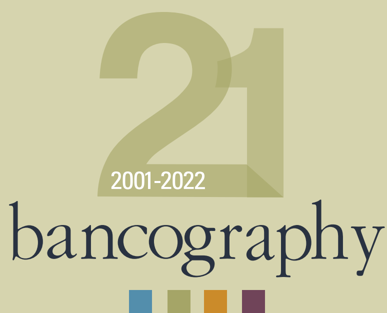

2022 New Branch Survey Findings: Size, Cost and Configuration

In 2003, Bancography conducted its initial survey of branch construction plans at U.S. banks and credit unions. We have reprised that study every three years since, pausing only during the lull in branch building that followed the financial crisis of 2008 - 2009. Each iteration of the survey inquired into four aspects of branch deployment: the number of new branches planned; size and format; cost; staff and equipment configuration.

Having most recently conducted the survey in 2019, 2022 brought us to our latest iteration. This year's survey panel included about 60 institutions, near evenly divided between banks and credit unions. Similar to prior surveys, respondents represented all regions of the nation, and all asset tiers except the largest national banks. The survey panel included institutions with fewer than five branches and several regional banks with more than 500 branches, providing a diverse audience against which to gauge industry trends.

Before presenting the results, a word of thanks to all our colleagues who committed the time required to complete the survey. Primary findings follow.

How many branches will your institution add next year?

Excepting the handful of respondents who indicated their institutions would not be adding branches in the year ahead, about half the panel cited incremental expansion efforts of one or two branches. However, some of the respondents from larger institutions remain more active, with about 15% indicating plans to add five or more branches in the next year.

These planned branch additions equate to an average increase of 4% versus current branch counts and a median increase of 8%. Note though, this does not address net branch counts, which may be declining as a bank or credit union closes more branches than it opens. Still, it reveals an objective of rebalancing networks – adding branches in high-opportunity markets even if also paring branches in overserved or lower-potential markets.

Seventy-nine percent of respondents plan to build traditional freestanding branches, 44% plan to build inline (i.e., within a strip shopping center) or other storefront branch models, and 8% plan to build in-store branches. Those proportions sum to more than 100% because many respondents intend to build branches in multiple service models, both freestanding and other types. In the 2019 survey, 72% cited plans to build freestanding branches and 36% inline, and the increase in both types suggests a greater use of mixed-model portfolios – versus sole reliance on freestanding or inline only. Overall, nontraditional branches (inline, in-store, or other specialty formats) represent 27% of all planned new branch deployments.

What is the average square footage of the planned new branches?

For freestanding models, the average size was 3,100 square feet, with a median of 3,000 square feet. Responses formed a classic bell curve, with two credit unions planning branches in the 5,000 square feet range, two banks planning freestanding branches at only 1,000 square feet, and a broad group in the 2,800 - 3,500 square feet range. Notably, there were no outliers in the 6,000+ square feet range, the first time that has occurred across the multiple iterations of the survey.

The 2003 study found an average size of 3,900 square feet, which decreased to 3,600 square feet in the 2006 survey and to 3,000 square feet in the 2013 survey. But the 2016 and 2019 surveys found medians and averages in the 2,800 to 3,000 square foot range, similar to this most

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recent iteration. This suggests the industry may have found a practical minimum for operational functionality, to effectively justify the land purchase and site preparation costs required for freestanding branches. Still, five institutions reported plans for new freestanding branches of 2,000 square feet or smaller, so there are those experimenting with more compact models.

The planned inline branches will feature an average size of 2,100 square feet and a median of 2,000. Both statistics remain within 200 square feet of the findings from the 2016 and 2019 surveys, again suggesting the industry has found a comfort zone with current models. Three-quarters of all responses to this question fell between 1,500 and 2,500 square feet, though two respondents cited models as small as 1,000 square feet.

What is the average land cost of the planned freestanding branches?

Because of the disparities in land values nationwide, this question usually shows broad variance in its responses, and that held true in 2022. Projected land costs varied from $250,000 to $3 million, but only two responses were less than $800,000 and only four exceeded $1.5 million; so, $800,000 to $1.5 million forms a reasonable, albeit broad range. The average cost was $1.2 million, the median $1.0 million. This represented the first increase in average land costs since the 2006 survey's $1.1 million average at the height of the branching boom. That statistic declined to $930,000 in 2016 and $750,000 in 2019.

The increase may reflect a general surge in prices across an array of asset classes since 2019. Or it may reflect some level of 'flight to quality,' to borrow a term from a different banking phenomenon: that in an environment with fewer branches overall and broader spacing between branches, banks and credit unions are bypassing second-tier submarkets and focusing only on the absolute top-tier locations. This reflects a model Bancography terms as "hub-and-hub," where institutions reserve physical deployments for a subset of top-tier, broader-spaced hubs, while relying on electronic channels to fulfill service needs in the in-between submarkets previously served by a second-tier 'infill' branch.

What is the average cost of the planned branches (including building, furniture, and equipment, i.e., everything but land)?

Outside of a few outliers, responses for total costs of freestanding branches ranged from a low of $550,000 for one of the smaller-format models to a high of $2.9 million. (There were two high-side outliers at more than $4 million, and a few low-side outliers of less than $500,000.) The average and median costs for planned freestanding branches reached $1.9 million, up a shade from $1.8 million in the 2019 survey, with most responses clustered between $1.6M and $2.5M. Average costs per square foot also inched upward, from $580/square foot in 2019 to $600 in 2022, with a median at $560/square foot. Eleven institutions projected costs of more than $800/square foot, including four at more than $1,000/square foot.

For the inline branches, costs increased more acutely, from an average of $675,000 in 2019 to $790,000 in 2022; and from a median cost of $540,000 in 2019 to $700,000 in 2022. These yielded average costs of $390/square foot (median $340), versus $350 (median $320) in 2019. There was broad variance in per-square-foot costs for inline branches, with three respondents citing costs exceeding $800/square foot but four reporting costs less than $200/square foot.

What are the planned initial staff levels for new branches?

Average branch staff expectations declined for both freestanding and inline branches, suggesting greater efficiencies in branch operations, or at least attempts thereon. For freestanding branches, respondents reported an average starting staff of 5.4 full-time-equivalent employees (FTEs), with 70% of responses falling in the 4 - 6 FTE range; the 2019 survey showed an average of 5.9 FTEs. For inline branches, respondents reported an average starting staff of 4.0 FTEs, versus 4.9 in the 2019 survey.

In addition to the declining staff counts in both models, the 2022 study revealed greater divergence in freestanding versus inline models. This suggests an increased emphasis on technology and reduced-cost operations at the inline branches, and perhaps a more defined demarcation between complex sales at freestanding branches versus simple service interactions at inline branches, matching the typical facility assignments in a hub-and-spoke branching model. (continued on page 3)

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The survey also addressed various equipment, configuration and design elements:

- For the first time, we omitted any question about **image-enabled ATMs**, as (per prior research) these are now ubiquitous in the industry.
- **Teller cash recyclers** are becoming standard, too; 80% of respondents plan to deploy TCRs at all new branches, and 85% in at least some new branches.
- Nearly half of all respondents (46%) plan to include **safe deposit boxes** in at least some of their institution's new branches, though only four respondents plan to include safe boxes in all new branches. Still, the 46% statistic represents an increase over the 35% levels found in 2016 and 2019; perhaps normal statistical variance, but possibly confirming the aforementioned hub-and-hub approach reflected in the increased land costs – i.e., some subset of branches employing a 'superstore' or 'flagship' model addressing all possible service needs.
- The COVID crisis created an immediate demand for remote-banking services, and this may have jumpstarted adaptation of **interactive teller machines (ITMs)** at the institutions offering such capabilities in 2020. However, the survey reveals only incremental increases in plans for ITMs. The 2019 survey indicated 26% of respondents planning to use ITMs at all new branches and 45% planning such in at least some new branches. In 2022, those figures edged upward, but only modestly, with 33% of respondents planning ITMs at all new branches and 50% planning such in at least some new branches.
- Of those respondents intending to deploy ITMs, 48% will utilize the ITMs in both **lobby and drive-in spaces**; 40% in drive-ins only; and 12% in lobbies but not drive-ins (and it is possible these branches cannot support drive-ins). In a point of greater consensus, 79% of respondents will operate their ITMs from a centralized call center, versus only 21% using in-branch staff to support the ITM interactions.
- Although service models with integrated teller/platform areas serviced by universal agents (often referred to as the dialog banking, or 'pod' approach) continue to take hold, the **traditional teller line** still retains a role in the industry's branch-design portfolio. Fifty-nine percent of respondents plan to eschew the traditional teller counter at all new branches, but 21% plan to include that feature at all new branches. The remaining 20% present a mixture of service models, where some but not all branches maintain the traditional teller-line element. For those aiming to use a model with integrated teller/CSR workstations, 85% also intend to cross-train all employees at those functions as universal bankers.

> ***The findings reflect an imperative of aligning the service model to the demands of a specific environment, versus deploying identical branch models in all markets.***

- In addition, although Bancography hears frequent conversations about the possibility of **cashless micro branches**, the reality of widespread use of such models appears further removed, as only six respondents cited initiatives to deploy cashless branch models in the next year. More prevalent is the branch as advisory center model, as 60% of respondents intend to include space for non-retail lines of business – such as wealth management, commercial banking or mortgage banking – at most or all branches; with the remainder reserving that capacity for only some of their new branches.
- Thirty-eight percent of respondents expect to outsource at least some proportion of **branch construction projects** to design/build firms – turnkey providers that manage all aspects of the construction process. Twenty percent will utilize design/build firms for all branch projects, 62% will hire and manage their architects and general contractors internally, and 18% will use a mix of construction management methods. These proportions remain similar to those found in the 2019 survey. A few respondents also cited a hybrid model, where a design-build firm developed an overarching concept for branch design that the institution then implemented via local architects for each specific branch.

In sum, while the overall count of branches nationwide continues to decline, many banks and credit unions still include new branches in their growth plans, even as costs for those branches edged upward. Of particular interest, land costs for new freestanding branches increased sharply from the previous iteration of the study, perhaps reflecting an intent to reserve freestanding branch investments for the absolute highest-tier submarkets only, while employing lower-cost service models in other submarkets. The industry also appears to have reached a practical minimum branch size level for the functionalities consumers and businesses demand, with most respondents affirming the importance of non-retail business lines, and only a few experimenting with micro-format, cashless service models.

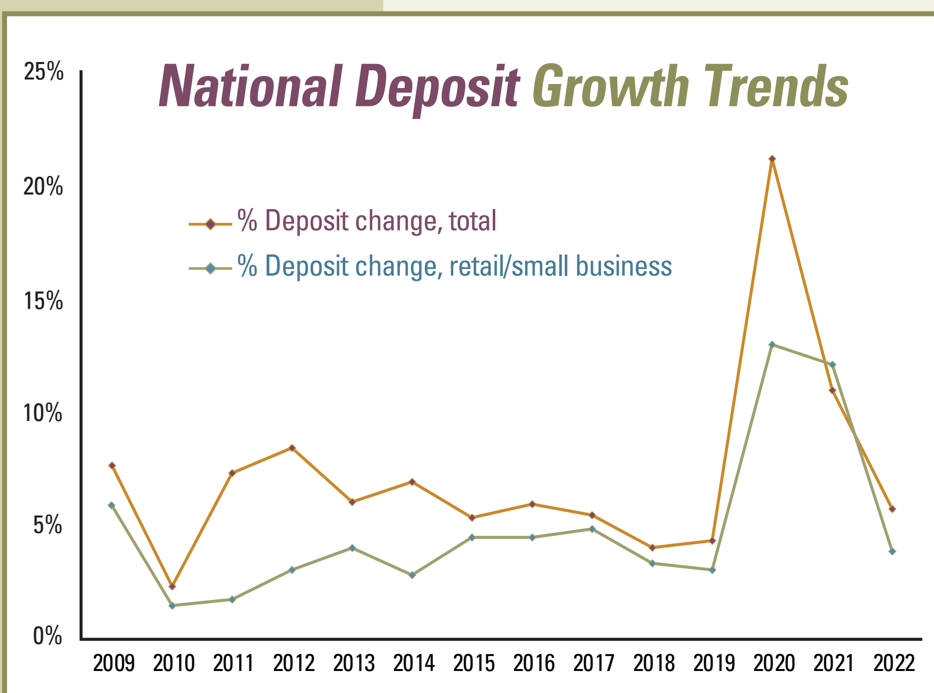
Finally, the survey reveals a need for bankers to consider a portfolio of service models, versus a single, homogenous approach at all branches. For example, many respondents plan a mixture of freestanding and inline branches, and a still significant 41% minority of respondents still plan a traditional teller line in at least some of their new branches. The continued relevance of teller counters, even if deployed more judiciously than in prior years, may reflect the importance of higher-volume business clients at some institutions. But in aggregate, the findings reflect an imperative of aligning the service model to the demands of a specific environment, versus deploying identical branch models in all markets.

Deposit growth did in fact slow, but it appears the industry escaped a period of flat deposit growth, and instead enjoyed the proverbial 'soft landing' back to historic deposit growth norms.

Findings from the 2022 FDIC/NCUA Deposit Statistics: Deposit Growth Normalizes

The 2020 and 2021 FDIC reporting years (the period ending on June 30 of the respective years) saw unprecedented deposit growth, with retail and small business deposit gains soaring past the 3% - 4% range typical of the prior 20 years and exploding to 13% in 2020 and 12% in 2021. The gains were fueled by two separate impacts of the COVID crisis. First, an array of governmental relief programs channeled funds into accounts; for example, proceeds from Paycheck Protection Program grants to businesses, and stimulus payments to consumers. Second, consumer outflows plummeted, as air travel, dining, retail shopping, and other activities diminished with consumers reticent to risk exposure to the COVID virus.

During the course of an array of branch optimization consulting projects in the past year, Bancography routinely cautioned clients that the 12% deposit growth rates of the past two years should not be viewed as sustainable or indicative of the pending environment. We also directed clients to expect flat or declining deposit growth in 2022 as consumers and businesses spend down surplus funds, followed by a reversion to the normal 3% - 4% deposit growth rates in 2023 and beyond.



We were close, and directionally accurate, but a shade too cautious. Deposit growth did in fact slow, but it appears the industry escaped a period of flat deposit growth, and instead enjoyed the proverbial 'soft landing' back to historic deposit growth norms.

In the 2022 FDIC reporting year (and including credit union data from the same June 30 period), retail and small business deposits grew by 3.8%, declining from 12.5% compound annual growth over the prior two years. Total deposits (which add large commercial and municipal deposits to the retail and small business category) increased by 5.7% in 2022 – again a sharp drop from the 15.9% average of the prior two years, though certainly not zero or declining.

The other headline finding from the FDIC's annual branch deposit reports relates to the number of branches in the industry overall. As electronic channels have gained traction, branch counts nationwide have steadily declined since peaking in 2011 at 113,000 branches. The 2022 reporting year saw continued erosion in branch counts to a nationwide inventory of about 97,000 branches, a net decline of 2,400 units from one year prior.

The net decline understates the number of branch closures, but may also give an illusion of branch construction ceasing. But looking below the top-line statistic reveals the 2,400-unit decline as the net impact of about 1,100 new branches opened, more than offset by about 3,500 branch closures. Those closures represent a mix of merger/overlap consolidations and strategic/profitability-based decisions.

Declining branch counts were not ubiquitous. Rather, some economically vibrant markets countered the trend of branch consolidation. Among the 55 U.S. metropolitan statistical areas with at least one million residents, Minneapolis, Nashville, Charlotte and Tulsa all showed increases in branch counts, even if by only a few units (as did Omaha, which falls just below the one million resident threshold). Other large metros, such as Salt Lake City, Albany, Oklahoma City, Raleigh, Jacksonville, Austin, Buffalo and Rochester, *(continued on page 6)*

What's Old is (Finally) New Again: A New Product Focus for 2023

The financial crisis of 2008 and 2009 and the recession that followed brought marked changes to consumers' personal balance sheets, and correspondingly to the balance sheets of banks and credit unions, too. On the liability side of industry balance sheets, the portfolio mix shifted dramatically. **Most notably, in 2008 CDs represented 38% of bank deposits nationwide; but that proportion eroded year after year, falling below 10% in 2020 and 2021.**

Consumers' loss of interest in holding CDs reflected, well, a loss of interest in CDs. In April 2009, the average yield on 90-day CDs across the U.S. fell below 1%, and then remained below 1% for a full eight years, finally breaking the 1% threshold again in May 2017. For much of that time, the average APY remained less than 50 basis points. It's really, really difficult for branch staff to capture the attention of consumers when the digit to the left of the decimal point in the rate board is a zero. Rates perked up slightly in 2018 and 2019, with the average yield on 90-day CDs even breaking 2% for most of those two years. But then the COVID crisis arrived, and rates returned to near zero for almost any product type – whether money markets, savings, or CDs.

But with 2022's round of Federal Reserve rate hikes, the yields available to consumers have revived. **And with substantial volatility in the stock market, many consumers may be receptive to the boring-but-stable guaranteed returns available from money market and CD products.** This change in sentiment creates opportunities for banks and credit unions, but institutions must prepare in order to leverage those opportunities. And keep in mind, if consumers would consider placing funds in a CD at your bank, they may also be open to moving funds from your bank to deploy at a competing institution.

Further, any branch officer who joined the industry in the past 12 years has never had to compete in a high-rate environment; never faced the challenge of convincing a depositor not to move their funds to a higher yield at the competitor down the street. **That negotiation process is critical, and requires training and role-playing exercises to learn, as well as some policy reviews.** How much latitude versus the stated rate is your institution willing to grant to branch officers? Any? Twenty-five basis points? If none, are there clear procedures for how a branch manager can request an override? And clear criteria for awarding those overrides, such as benchmarks for client balances, tenure, or profitability?

Bankers must also consider the appropriate sales tactics to attract or retain balances even without matching the top-of-market rate. This can include sales scripts with which the officer can remind the client of the bank's other benefits, or relationship-pricing protocols (e.g., we can't match Metro Bank's rate on this CD, but if you place/keep the funds with us, we can provide a fee-free premium checking account).

> *In times of uncertainty it remains incumbent that a trusted banker maintains an ongoing dialog with customers and introduces potentially beneficial products as appropriate.*

This author once had lunch with a bank president in a prototypical college-town market, saturated with community and regional bank competitors as such markets often are. Counting at least 12 branches on our brief walk from the bank's main office to the restaurant on the town square, I asked how his bank could possibly compete, and the banker replied **"we have great customer service…I know everyone says that, but we really excel in knowing every customer personally, and as a result our clients are loyal to within 50 basis points."** What was most fascinating, this bank president had quantified the rate deficit his clients would tolerate. He had gauged from experience that if the bank across the street was offering 4%, the bank's brand and service premise were strong enough that clients would remain if they could get to 3.75%, or 3.5%…but at 3.25% no level of stellar service could save the relationship.

It's an important framing of the challenge: we all can't offer the highest rate in town, so for those that don't lead on price, what other attributes are keeping your clients loyal, and how much of a pricing deficit can those attributes offset?

Irrespective of your institution's pricing position, bankers can gain relationships by means other than waiting for consumers to walk through the branch doors. **A volatile stock market creates uncertainty for consumers, and often creates a 'flight to quality' to stable, insured deposits.** So, for current clients, have branch officers initiate contact, calling customers or members simply to apprise them of the guaranteed rates they can now lock in – versus the volatility and uncertainty of the stock market. Don't assume your clients are aware of the current rate offering; remember, they've become conditioned to see CDs and money markets paying imperceptibly low rates. It may take a phone call to inform them that your bank is now offering 4.5% yield; and those clients will be grateful for the knowledge, and more likely to view the branch officer as a trusted advisor going forward.

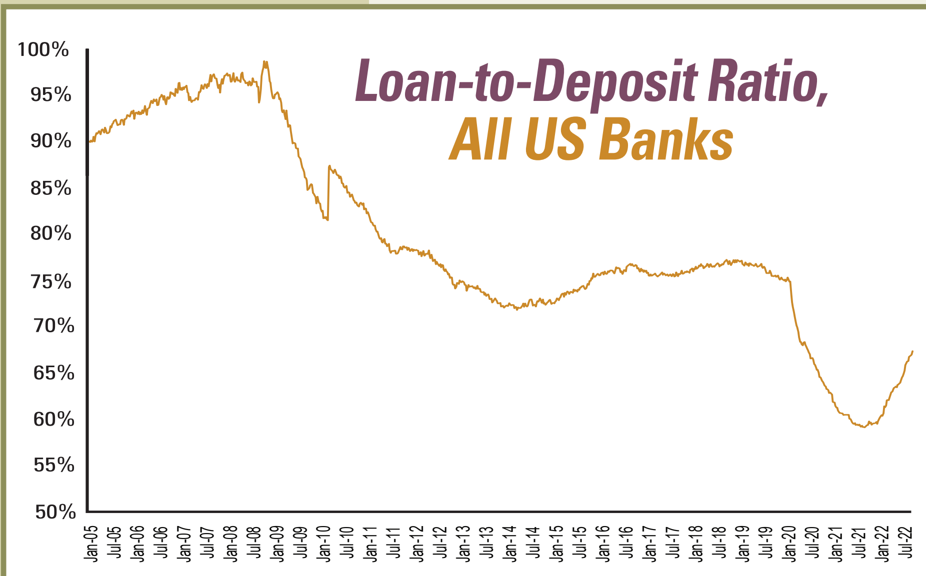
Just as CDs present a revived opportunity on the liability side of the balance sheet, home equity lines present similar potential on the asset side. At the onset of the financial crisis, U.S. consumers carried nearly $1.1 trillion in balances in home equity lines and loans. However, in the aftermath of the financial crisis, many banks reduced HELOC borrowing limits or opted not to renew some equity lines (in some cases declining home values eroded the equity against which consumers could borrow). And consumers, chastened from overleverage that brought them to the brink of insolvency and losing their homes, turned much less likely to borrow against already diminished home equity.

Even as home values recovered and consumers regained equity in their homes, the HELOC remained unwanted, and balances eroded year after year. By the end of 2021, aggregate home equity lines and loans at U.S. financial institutions had fallen below $400 million; the industry saw $800 million dollars in that product disappear from its collective balance sheets. In more recent years, the decline in home equity balances reflected consumers' replacement of the HELOC with cash-out refinancings. With many consumers in the past five *(continued on page 6)*

The 2022 FDIC/NCUA Deposit Statistics: Deposit Growth Normalizes (continued from page 4)

showed minimal impacts, with net branch counts remaining flat or declining by only a few units.

In contrast, the New York metro area experienced a net decline of more than 200 branches over the past year, representing a 4% contraction from 2021 branch inventories. And the Washington, DC metro saw the net decline of more than 100 branches, equating to a more severe 6% reduction in aggregate branch counts. Chicago, Los Angeles and Detroit all posted net reductions of 80 to 90 branches over the past year, a 3% change in the former two but a more severe 6% decline in the latter. The Philadelphia, Boston and Miami metros also experienced significant branch consolidation, each with net declines of 60 to 70 branches since 2021; and in each case representing about a 3% reduction in total branch counts.



The return of deposit growth to more historically normal levels brought the benefit of allowing banks and credit unions to absorb excess liquidity. The unprecedented rise in deposits, coupled with a COVID-driven slowdown in borrowing – especially in the commercial sector – cratered the banking industry's loan-to-deposit ratio to only 59%, the lowest level on record (at least within the history of the Federal Reserve Board's available data tables, which date to 1973). The industry's loan-to-deposit ratio began to trend upward again in the third quarter of 2021 and has now revived to 67% (November 30, 2022), recovering all the ground lost since August 2020, but still lagging the 75% industry-wide level at the onset of the pandemic. Still, with the surfeit of deposits finally eroding, liquidity trends appear favorable, as illustrated in the graph to the left.

In sum, the moderating pace of deposit growth appears favorable for the industry, and while a trend of branch consolidation nationwide continues, the competitive branching environment varies broadly across regions and markets. Bancography's 2023 Outlook, to be published in February, will explore deposit, branch, and other industry trends in more depth, at both a nationwide and market level.

What's Old is (Finally) New Again: A New Product Focus for 2023 (continued from page 5)

years facing an opportunity to lower their interest rates via refinancing, why not refinance more than the amount owed, and take what amounts to a home equity loan with no additional fees for paperwork required?

Now, with mortgage rates rising and a sizable proportion of homeowners already refinanced to lower-than-current rates, **the HELOC once again becomes an attractive vehicle for borrowing; and with higher overall rates, the tax advantages of HELOC borrowing become more valuable.** Reflecting that, home equity balances have finally started to trend upward, albeit modestly. After reaching a nadir of $390M in the first quarter of 2022, aggregate U.S. home equity balances increased to $405M in the second quarter and to $419M in the third quarter. *(Note: all data in this section are from the Federal Reserve Board's Flow of Funds Accounts tables).*

As with the CD case, consumers may not know the benefits or existence of home equity borrowing products, and those who are not aware of the product will not learn of it automatically. Rather, it remains incumbent that their trusted banker maintains an ongoing dialog and introduces potentially beneficial products as appropriate.

In sum, changes in the economic environment create changes in consumer needs, and bankers who recognize these changes and take the initiative to share implications with clients can gain not only balances but also client appreciation and loyalty. In today's environment, a reminder call about the benefits of long-forgotten CDs or home equity lines may give an inroad for such mutually beneficial product sales.