Branch Visits Fewer, But Ever More Important by Dave Martin – 6/5/13 (American Banker)

The term "showrooming" has been coined to describe the phenomenon that has folks decoupling where they shop from where and how they buy.

What was once mostly a practice of techies has become mainstream and is impacting retailers from mom-and-pop stores to giant discounters. And while shopping for bank products doesn't require hands-on inspection or a store (branch) visit, these new behaviors are affecting us as well.

Growing numbers of shoppers are using stores as showrooms to physically inspect items and then search for better deals on those products online. I've seen my wife scan an item with her smartphone, search for it online and purchase it from another online retailer while we stood there in a store. I walked out feeling I should be handing someone a tip for use of their facilities.

Recent research suggests that as many as one-in-five retail customers are now showrooming, with one-third of those shoppers leaving stores and purchasing elsewhere online. And the practice is growing quickly, with over 90% of smartphone owners saying they plan to "showroom" in the future. Fair or not, this is the new reality for most retailers and portends a sea change in how folks shop for all manners of things.

The music store where my younger son takes lessons has begun including the "online price" followed by the "store price" on their guitars' price tags. The store price always matches the online price. When I kidded with the manager about that fact, he told me that in the last couple of years, people walk into his store, test guitars off of his wall, take pictures of them, and then shop for them online. He explained that he actually wants a customer to question him if he finds a lower price online. He then at least has a chance to either match the price or explain to a customer why spending a few more dollars with him would be worth it. The manager says that if he can get folks chatting about "musician things" he has a better than average chance of establishing at least some kind of connection with them. Then, he's not simply the guy charging more than the faceless guys online.

Something that many smart retailers like this manager have learned is that they cannot afford to sit back and not engage customers in their presence. If no personal connection is made with a shopper, purchase decisions often come down to price. And customers now have instant and complete pricing information at their fingertips.

I often talk about issues like this with banker groups to make the point that folks now have their most trusted advisor always with them, right in the palms of their hands. On occasion, a banker will remind me that I've stated previously that friends and family are shoppers' most trusted advisors. I then point out, "Well, how do you think they communicate with them?" Whether someone is performing a Google search or texting a friend, the dynamic is the same.

Today's mobile technology encourages and enables higher levels of skepticism and scrutiny by customers than ever before. But technology doesn't tilt the playing field. It levels it.

As some begin to feel a little depressed about the idea that our businesses seem to be heading inescapably to a low-cost provider competition, I suggest that no bank is going to differentiate itself purely on pricing over the long haul. We're going to charge what's fair to customers and sustainable to us, and everyone will be in the same ballpark.

But as our products, and even the way they are shopped for, become more homogenous and technology driven, the way customers "feel" about doing business with us takes on more importance than ever. Our branches (of whatever type, size and location) will either be our competitive advantage or our albatross.

If we allow customers to experience a branch visit as they typically experience a post office visit – a necessary evil – we practically encourage them to shop elsewhere when considering their next financial need. If nothing about a visit makes me feel respected, or informed or appreciated, why would I be particularly interested in bringing more of my business there?

While face-to-face interactions may be nowhere near the most common banking transaction these days, they continue to have an inordinate influence on how customers think and feel about a bank. We cannot afford to waste them.

<u>Are customers in and around your branches today sensing that you value and appreciate the fact that they are</u>? **Strive to make any interaction with one of your bankers the friendliest and most professional contact a customer has with any service provider today. Their search for a trusted banking relationship will end with you.**

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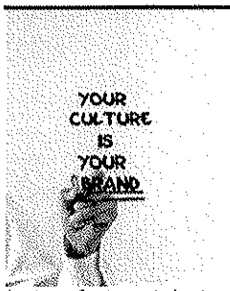
PROTECTING THE BRAND AS YOU EVOLVE THE BIZ:



If you want to see how much reputational risk can result from significant changes to a business model, look no further than JC Penney. Some time ago, the venerable retailer was concerned about losing market share in a changing world of retail sales, so they brought in a new CEO. They hired former Apple Stores leader Ron Johnson who promised to give Penney's a younger, hipper image. Johnson made big changes but unfortunately took a tone deaf approach to the store's core customers. Marketing shifted, discount coupons were eliminated and new pricing showed up on merchandise. The results were catastrophic as customers stopped coming in, sales tanked and Johnson was eventually fired. In his place, the board brought back a former Penney's CEO, who has been apologizing in the media and asking customers to come back ever since.

To armchair quarterback what happened, it doesn't seem like changing the look and feel of the stores or even pricing were the primary culprits. It seems more likely that management just didn't understand what made customers shop there, what they liked about the store and what they didn't like.

Community banks are facing a similar dilemma to department store retailers, as the landscape of business changes. This publication regularly extols the virtues and even necessity of having the technology and modern trappings to attract and keep sophisticated customers, but there is a balance. While striving to update and be relevant in the technology-driven world, community banks must never forget their core customers. Take the time to understand what is most important to those customers and be absolutely certain to maintain the qualities that drive them to your bank.

The data shows fewer bank customers are coming into branches and more are using the internet and/or mobile applications to do some of their banking. That said, customers still come into branches, primarily to do more complex business, so carefully analyze any moves before plunging into what could be very cold water indeed with major changes. Many of the largest banks still have a broad branch network, but there are often very few people in those branches and the staff is unqualified or unable to make many decisions. We wonder if the customer seeking to do more complex business that comes into the branch is getting the sort of service they are seeking. No wonder customers look online for solutions.

For community bankers, things aren't quite that out of control just yet. The community bank model is built around strong customer service and that is at the very core of what drives customers to do business with you. No matter the twists and turns of technology, be sure your branches have qualified, empowered people to take care of your customers and augment that with services to keep you relevant. Sure, people may come into the branch these days with a different viewpoint than they had 10Ys ago, but there are many more twists and turns yet to come before the branch totally goes away.

As JC Penney learned the hard way, building a solid reputation takes a long time, but tearing it down can occur quickly. Our advice is to be unafraid of change and embrace it, as you tinker with things and slowly evolve the business over time (rather than switching everything all at once). Your culture is your brand, so protect it, as you continue moving toward a changing future.

ECONOMY:

- **No significant economic data is scheduled for release.**

FIXED INCOME & RATES:

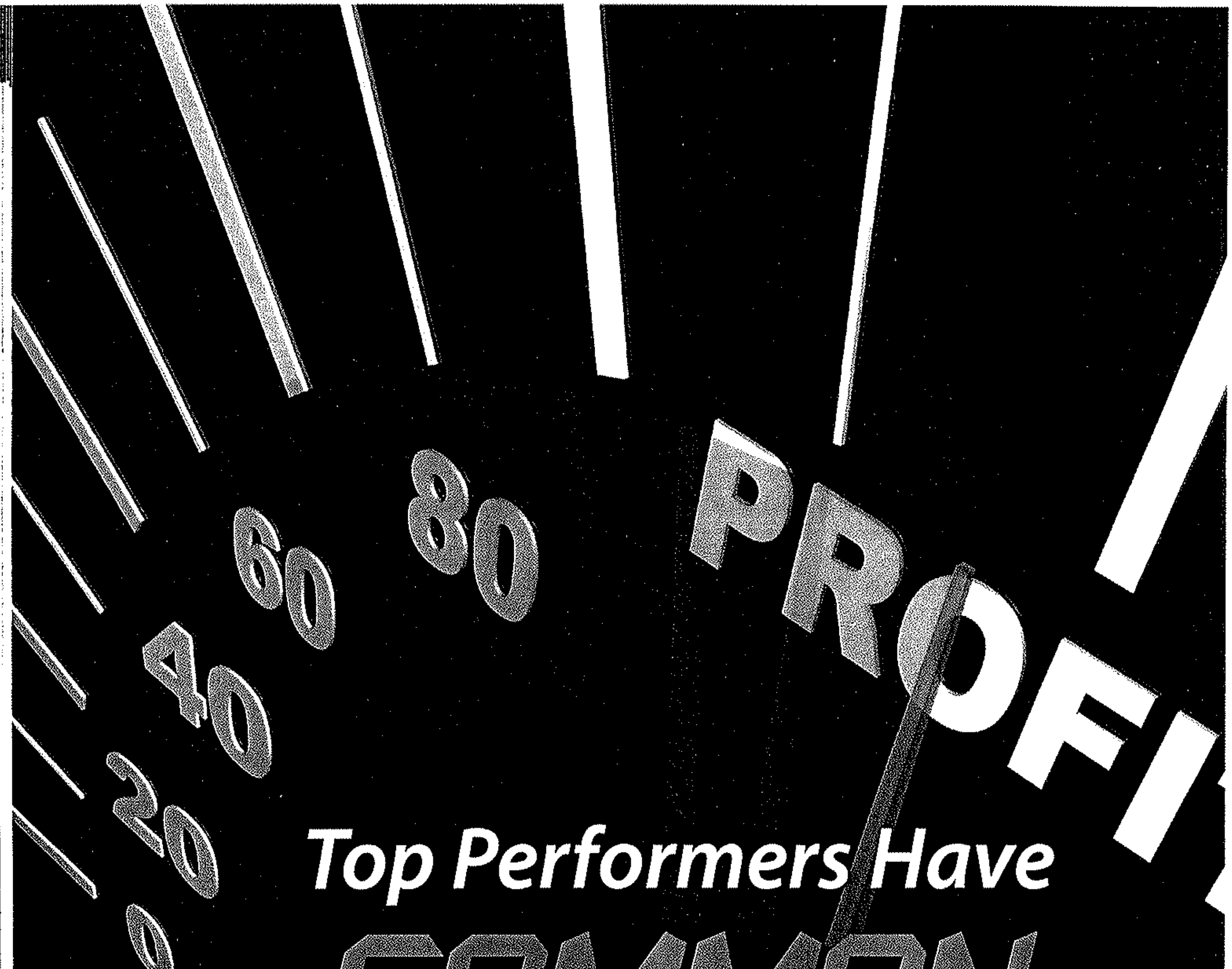
Yesterday: Yields rose less than 1bp, helped by stronger-than-predicted jobless claims. **Today:** Demand for safe-haven Treasuries has sunk due to strong equity gains, driving yields up 3bps so far this morning.

BANK NEWS:

- **Warning**: An astute regulator reminds us that yesterday's article on targeting women with a program supported by financial advice should have included a reminder that gender is a protected class under all fair lending laws and fair treatment guidelines so be sure to consult with your compliance or legal staff on any new programs to avoid issues with discrimination.
- **Rate Risk:** The Financial Times reports many of the top US universities have cut back endowment holdings of US Treasuries from as much as 30% in 2008 to as low as 0% in some cases. Endowment managers say they took the action because they are worried about the impact of rising rates.
- **Lending Pressure**: JPMorgan reports junk bond yields have fallen below 5% for the first time ever as more and more investors chase yield. While not directly related, this pressure is also translating into the lending arena of community banks, with many telling us they are trying to hold the 4% level on longer term CRE loans, but seeing the largest banks dip in on some relationships with pricing as low as 3% now.
- **Foreclosures:** RealtyTrac reports foreclosure activity in Apr. hit the lowest level in 74months, as the housing sector gets better.
- **Mobile**: The latest research by the Wireless Industry Association finds 34% of US households as of 2011 only use wireless phones, as land lines go the way of the dinosaur.
- **Mobile**: Cisco reports that as of early 2012, the percentage of people in this country who owned a smartphone passed the 50% level.
- **Capital**: Reuters reports more companies are raising capital by issuing shares "at the market." This term refers to selling stock on the open market, at the current price, usually in small amounts and over weeks or months (vs. selling a bigger chunk all at once). The cost to issue these sorts of offerings are reportedly 2% of money raised vs. 4% to 5% for more traditional methods. If you are seeking capital and have enough liquidity in your stock, you might want to consider this method as a less expensive option (even Bank of America did this recently).
- **Location Aware Marketing**: In the world of mobile technology offerings, banks should note this term refers to the process of delivering online content (such as targeted marketing data based on proximity to a business) to users based on their physical location (leveraging phone GPS technology).

Tsy Yields & MTD Chg			Libor Rates		3ML Swap		Expected FF	
3M	0.04	-01	1M	0.20	2Y	0.37	6/19	0.12
6M	0.07	-01	2M	0.24	3Y	0.49	7/31	0.12
1Y	0.11	+01	3M	0.28	4Y	0.69	9/18	0.12
2Y	0.23	+02	4M	0.32	5Y	0.93	10/30	0.12
5Y	0.77	+09	5M	0.37	7Y	1.42	12/18	0.12
10Y	1.85	+18	6M	0.43	10Y	2.00	1/29	0.13
30Y	3.05	+17	1Y	0.70	15Y	2.56	3/19	0.14

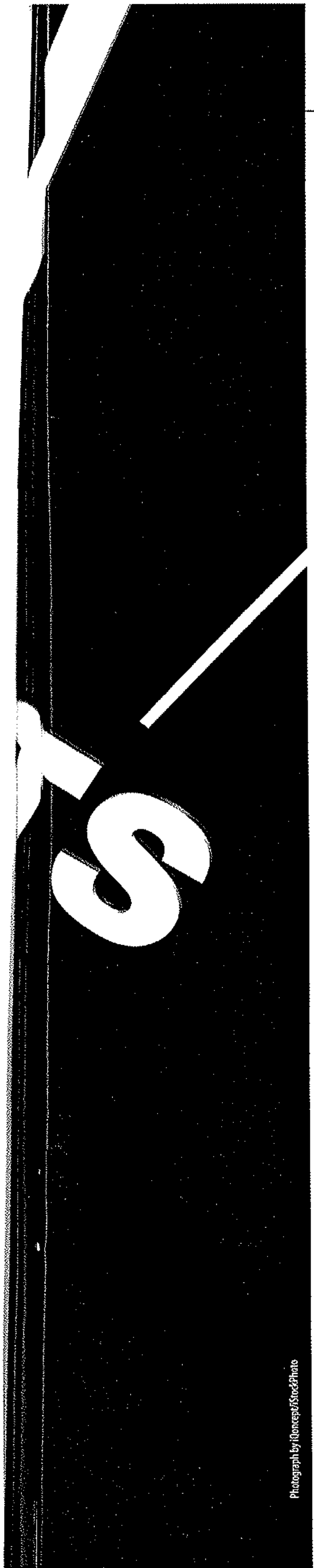
O/N Libor	Prime	FOMC Rate Hike @ 6.5% Unemployment Rate	
0.15	3.25	Apr 2013: 7.5%	Mar 2013: 7.6%



Top Performers Have
COMMON TRAITS

Each year for the January issue, *BankNews* interviews CEOs of some high-performing community banks across the nation. On the following pages, bankers from Iowa, California, New York and Michigan share thoughts about their success.

By Elizabeth Whalen



Photograph by iDoncept/iStockPhoto

Although four of the highest-performing community banks from around the country appear very different, they have actually built their success on similar foundations of efficiency, cautious lending and investing practices, and specialized expertise.

Pocahontas State of Pocahontas, Iowa, carefully manages its $92 million asset operation: Its efficiency ratio is in the 16 percent range, far lower than the community bank average of about 68 percent, according to President and CEO Robert F. O'Donnell.

"It's having the right people who do their jobs and do them well. Everybody does more than one thing," he said. All his employees are cross-trained on each others' jobs so that, if necessary, the bank can operate effectively with half its normal staff of nine. That efficiency helped Pocahontas State place 11th on SNL Financial's list of the 25 best-performing community banks of 2011.

Chartered in 1926, the bank brings that same level of control of its costs to its lending and investment policies. In fact, the bank had only one problem commercial loan throughout the recession and was eventually able to recover the entire amount it had lent.

For real estate, the bank funds only conventional loans of no more than 80 percent of the property's value, and the bank itself makes the final determination of what that value is.

"If the appraisal comes in higher, it's still 80 percent of what I feel the property is worth, just from experience and knowing what the market is in the area," O'Donnell said.

That experience led Pocahontas state to avoid mortgage-backed securities.

"I wouldn't buy those even before things crashed," he said. "You can't be lending more than a property's worth, and we saw that happening even in this area. You would see the filings go through at the courthouse, and you'd just stand there and shake your head because it might be twice what that property would command as a price if you were selling it."

Vibra Bank of Chula Vista, Calif., also has no non-performing loans, according to President and CEO Scott Parker. The bank, which opened in July 2008 and now has $115 million in assets, does not offer mortgage lending, but does provide commercial real estate and Small Business Administration loans along with home equity lines of credit.

"We underwrite cautiously and prudently," Parker said. "Obviously, it's easier to make money if you're not charging off loans, and our loan quality is extremely high."

Parker attributes Vibra's success, which includes earning a Super Premier Performance Award from Findley Reports, to loan growth and the bank's focus on the relatively underserved bicultural market: Chula Vista is about seven miles from the border with Mexico, and 75 percent of the area's residents are Hispanic. The bank was founded to serve that market, especially its businesses and professionals.

The bank gets its "cultural credibility," as Parker puts it, from the fact that many of its directors and founders are originally from Mexico. As a result, Vibra offers its customers more than just a bilingual staff.

"For instance, it's not a huge part of our portfolio, but we will look at and consider income derived from Mexican sources in our overall credit analysis," he said.

Vibra's primary source for establishing repayment ability remains U.S. tax returns, Parker said, but the bank will look at Mexican tax returns as a secondary information source.

"We're able to at least incorporate that information into our overall understanding of the borrower and their overall financial picture," he said. "That's something that most banks don't do."

Because Vibra Bank is relatively new, it has not made any post-recession operational changes. Parker has worked in banking since 1986, and he believes Vibra will need to continue to find ways to differentiate itself in order to remain a high performer. Similarly, O'Donnell said that Pocahontas State has no plans to make significant changes to its business model in order to maintain its high performance.

The same is essentially true for USNY Bank, of Geneva, N.Y., which opened in July 2007 and now has $137 million in assets, according to Mike Briggs, president and CEO.

"I don't really know where the future's going to go, but I think opportunities are going to be there for banks that have good capital, have a good team, have good performance."

"It's the same people doing the same thing with the same business plan in the same market with the same type of customers. Other than adding a little bit of a focus on residential mortgages, the bank's really the same as it was when we opened."

The bank, which ranked 20th on SNL's 2011 list of best-performing community banks under $500 million, recently added residential mortgages as a focus, not because it was initially avoiding the business line but because it was busy managing all the other aspects involved in founding a bank.

"Once we got through that, we realized that residential mortgage activity could be and should be an integral part of a community bank in our markets," Briggs said. "In 2012, we've generated over $350,000 in residential mortgage premiums, so those fee income pieces are important."

USNY primarily focuses on commercial agribusiness and agriculture and provides SBA and Farm Service Agency loans. Loans through those programs brought the bank more than $300,000 in premiums in 2012, according to Briggs.

SBA lending is growing in importance to Crestmark Bank of Troy, Mich., a business-to-business lending institution with $430 million in assets that, since its 1996 inception, had mostly focused on asset-based lending and factoring.

"We're diversifying and expanding our product offerings. We were exclusively a working capital type of shop, mainly doing accounts receivable and inventory financing in the past. Over the last year and a half, and going forward, we're adding other alternatives, such as the SBA program. We also have a leasing program, an equipment term loan program, just to name a few," said Chairman and CEO W. David Tull.

Crestmark's focus on high-margin businesses generates a net interest margin of about 15 percent, a figure many traditional banks might envy, said Tull, but that increased margin carries costs, too.

"Our asset management operating expenses are higher than most traditional banks' because we have to monitor our accounts much more closely, but our efficiency and our deposit gathering help make up for some of those added expenses. If you keep your charge-offs at reasonable levels, then it falls to the bottom line, which is what happens in our case," Tull said.

To ensure Crestmark's charge-offs remained low during the recession, the bank analyzed the financial status of its clients and those clients' customers.

"For example, in the automobile industry, in which we had fairly large exposure, we looked at what vehicles our clients' products were going toward. If they were going toward the Hummer, it was a lot higher risk than if they were going toward another car. That would obviously make a big difference as to the potential collectibility. By doing that, we were able to support all our automobile clients throughout the recession."

That careful examination of its clients helped Crestmark rank as one of SNL's 2011 best-performing community banks under $500 million.

Now that the country is in recovery mode, USNY's Briggs believes that today's strong banks will be in the best position to grow along with the economy.

"I don't really know where the future's going to go, but I think opportunities are going to be there for banks that have good capital, have a good team, have good performance." BN

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From High Tech to High Touch

Banks need to pay attention to Gen X and Gen Y

Banks have made a major commitment over the past few years to new technologies designed to better serve their current customers, as well as to attract new customers wanting the latest and greatest services — from mobile banking and remote deposit capture, to person-to-person payments and personal financial management tools.

Although this strategy is on the right track, it may be missing one important element: the human element. According to a recent research study, Gen Y (those ages 18–32) and Gen X (those ages 33–48) consumers do not necessarily want high-tech solutions in isolation; rather, they want the benefits of new technology in tandem with support, advice and more knowledgeable people to help them manage their money.

"While new technology is important," said Andrea Simon, corporate anthropologist and founder of Simon Associates Management Consultants, "it is simply not enough for many Gen-Xers and Gen-Yers/Millennials. These groups are not averse to mobile banking, digital coupons and smartphone apps, but many need to know there are real people at real institutions helping them to manage their real (and future) money."

Gen X is now in the prime of their careers. They are making and investing money, and seeking financial advice to plan for their futures. The first wave of Gen Y — those between ages 25 and 32 — is in the stage of life where establishing financial goals and developing banking relationships are becoming important. Fortunately, these groups believe in and trust banks, both from their own experience and the experience of their parents. Their trust may be waning, though, because of banks' perceived move away from personal interactions.

"Satisfying transactional or functional needs without emotional connections creates limited value," said Simon. "The challenge for banks is realizing that the old model is broken, and that Gen-Yers and Gen-Xers could help them create a new one based more on how people buy — through emotions."

Traditionally, branches have helped customers connect in a more personal way. Yet many banks have closed or plan to close branch locations in favor of more cost-effective and efficient omnichannel banking, thought to be the preference for younger generations. This may be short-sighted, however.

A recent Javelin report, for example, found that older Gen-Xers prefer to conduct transactions at branches at a rate 2.5 times greater than those over the age of 65. Although 56 percent prefer to monitor accounts and balances online, a surprising 25 percent still visit branches for these activities. As Javelin's Mark Schwanhausser, one of the report's authors, puts it, "They need some hand-holding."

Simon points out that branch banks are billboards and brand builders, albeit expensive ones. And even though some 2,000 branches were closed last year, according to SNL Financial, the number of branches now is four times the number in 1970. Yet the debate about the future of the branch rages on, focusing around two major viewpoints: Branches will eventually perish largely because an in-person branch transaction is far more costly than an online transaction ($4.25 vs. $0.10); and, if branches do survive, they will need to become more consultative, with a knowledgeable staff capable of helping customers with financial guidance.

This second view coincides with Simon's finding that banking is still a people-to-people business and banks must not lose sight of this.

"Banks need to go well beyond the functional transaction," said Simon. "They need to become familiar, respected and knowledgeable investment advisers that can take a personal and professional interest in their Gen X and Gen Y customers — and their futures." BN

Image courtesy of Ryan McVay/ Digital Vision/Thinkstock