

The Finance &
Accounting Forum
For Financial Institutions



Branch Transformation Strategies

Monday June 13, 2016

1:30 p.m.



Presented by:

Jeffrey L. Morris

Managing Director & Principal

Austin Associates, LLC

Toledo, Ohio

(419) 317-1775

jmorris@austinassociates.com

www.austinassociates.com

www.loanpricingpro.com



AUSTIN ASSOCIATES OVERVIEW

Consulting and Investment Bankers to Community Banks



- Community bank advisors for more than 50 years
- Specialized services through multiple practice areas

Investment Banking

Strategic Consulting

Financial Management

Technology Solutions

- Owners are consultants/managers
- Over 200 bank/thrift clients in 2015 from 28 states
- Nationally-ranked leader in community bank M&A for 3 decades



AUSTIN ASSOCIATES OVERVIEW

Financial Management Consultants for Financial Institutions

- Specialized services from the Financial Management Division

Asset / Liability Management

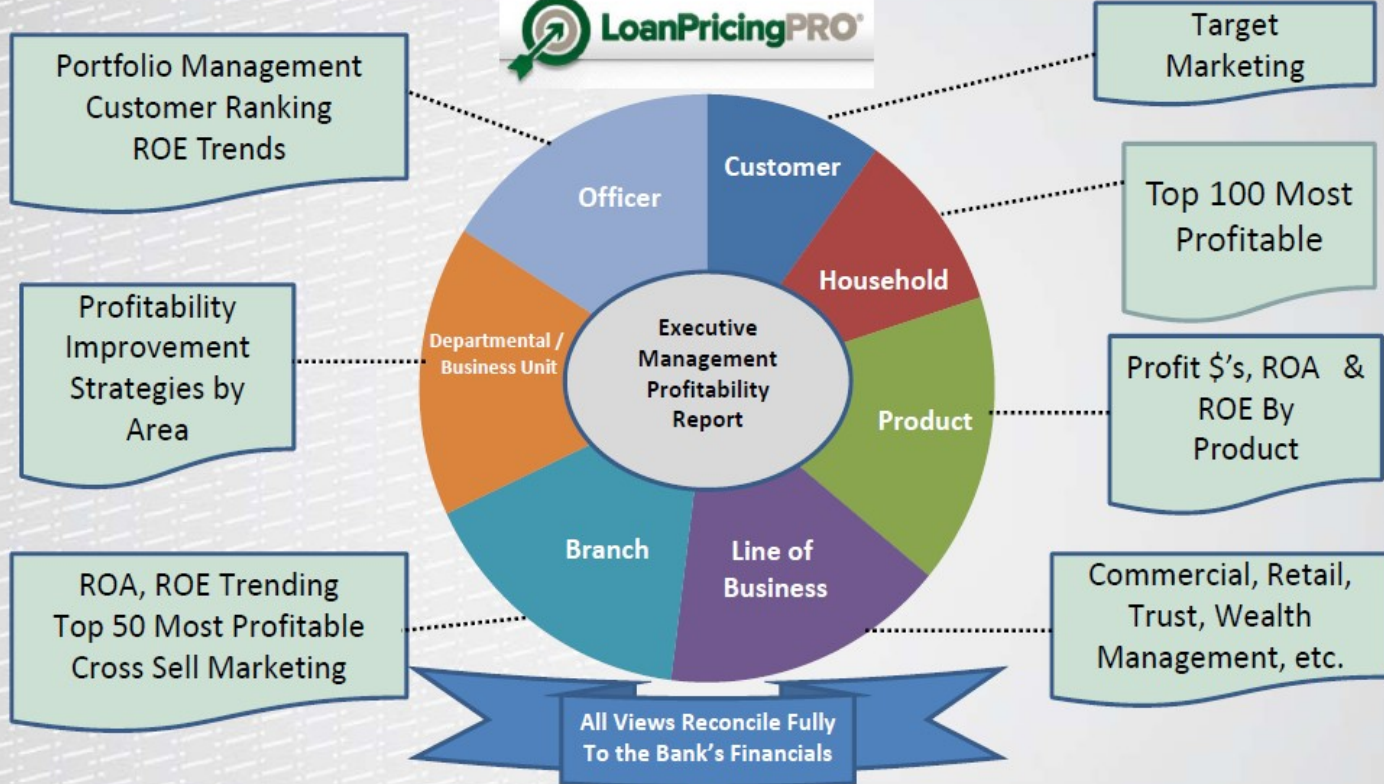
Profitability Measurement & Improvement

Loan & Relationship Pricing Systems

Balance Sheet Structuring

Regulatory Compliance

The Austin Profitability System



Core System Data Funds Transfer Pricing Salary Cost Allocation Non Salary Cost Allocation
 Allocation of Credit Risk (PFL) Non-Interest Income Allocation

*****CONSULTING*****

The Finance & Accounting Forum
 For Financial Institutions



AGENDA

Branch Transformational Strategies

June 13, 2016

- I. Business Trends Affecting Retail Industry
- II. Bank Industry Trends Affecting Branches
- III. The Branch's Impact on Bank Profitability
- IV. Do-it-yourself service
- V. Today (and tomorrow's) customer
- VI. Transformational Strategies

Branch Transformational Strategies

June 13, 2016



I. Business Trends Affecting Retail Industry

WHY LOOK AT THE RETAIL INDUSTRY ?

- Evolution of technology is advanced vs Community Banking
 - Effect of on-line retailers – Amazon, Ebay
 - Point of sale systems, data mining, pop-up offers, chat rooms
- Effect of Millennials seen earlier than in banking
- Easier to recognize patterns in other's industry
- Potentially predictive of where trends may take us

7

Struggling Ralph Lauren Tries to Fashion a Comeback

Percentage of operating profit
and sales from department
stores and specialty stores



THE WALL STREET JOURNAL.

Recent Troubles

- Sales are flat
- Profit down 50%
- Market value was \$16 B, now \$8 B



New CEO, formerly at Old Navy, hopes to revive company by closing stores, trimming management and reducing discounts

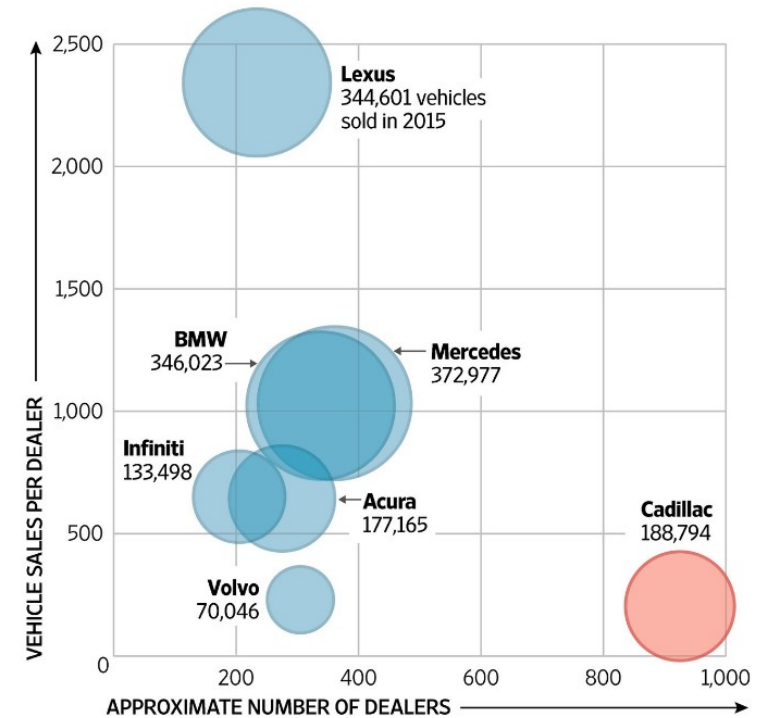
Cadillac Bets on Virtual Dealerships

A portion of stores for GM's luxury division will become showrooms with virtual-reality headsets and no cars



Large Dealer Footprint

Cadillac sells fewer vehicles in the U.S. than many luxury-car rivals but has far more dealers.



Sources: the companies; McKinsey; Automotive News
THE WALL STREET JOURNAL.

Amazon Dash Button



BUY DASH BUTTON FOR \$4.99 AND **RECEIVE A \$4.99 CREDIT** AFTER YOUR FIRST PRESS

70+ New Dash Buttons



amazon echo

Always ready, connected, and fast. **Just ask.**



CHRISTMAS SHOPPING - 2015



THE CHRISTMAS SHOPPING SEASON - 2015

More people
shopped
ON-LINE than
in STORES
during
The Thanksgiving
and Black Friday
weekend, 2015

- National Retail Federation



CHRISTMAS SHOPPING, 2015



Black Friday ON-LINE sales

\$4.45 Billion

Now 27% of total Black Friday Sales

Up 14% from 2014



57% was on MOBILE devices

Up over 100% in one year

- Adobe System Inc.

RETAIL INDUSTRY TRENDS



- Brand entrants are more focused
- Stores shrink
- Giants personalize and localize
- Frenemies collaborate
- Global brands embrace social issues
- Narrowing & broadening

Source: PwC's Retail and Consumer Trends - 2016

15

Technology, and Other Trends Affecting All Retail Service Providers



- I. Banking as a *Social* Experience
- II. Millennials are setting the tone for the future
- III. Mobile is the medium
- IV. Omni-channel equals a seamless experience
- V. Big data can uncover unprecedented insight

The Impact of E-commerce on Retail

E-commerce has been steadily growing for several years, and is expected to hit ***\$327 billion in 2016***, up from \$202 billion in 2011. More brick-and-mortar-focused retailers are stepping up their online game and increasing the percentage of their sales that come from online channels, and web-only retailers have been growing at an impressive clip, too.

Why E-commerce is growing so rapidly



We are busier than ever and want things faster and easier with less commitment. We want personalized experiences that account for our preferences and constraints.

Source: Bryan Eisenberg,
Founder & CMO, IdealSpot

18

Branch Transformational Strategies

June 13, 2016



II. Bank Industry Trends Affecting Branches

BANKING INDUSTRY TRENDS



- Increasing competition
 - Other community banks
 - Regional & National Banks
 - Credit Unions
 - Non-bank providers (Fintech)
- Growing Influence of Millennials , decline of Baby Boomers
- Weak economic conditions / low demand
- Persistently low interest rates
- Evolution of Technology

20

BANKING INDUSTRY TRENDS

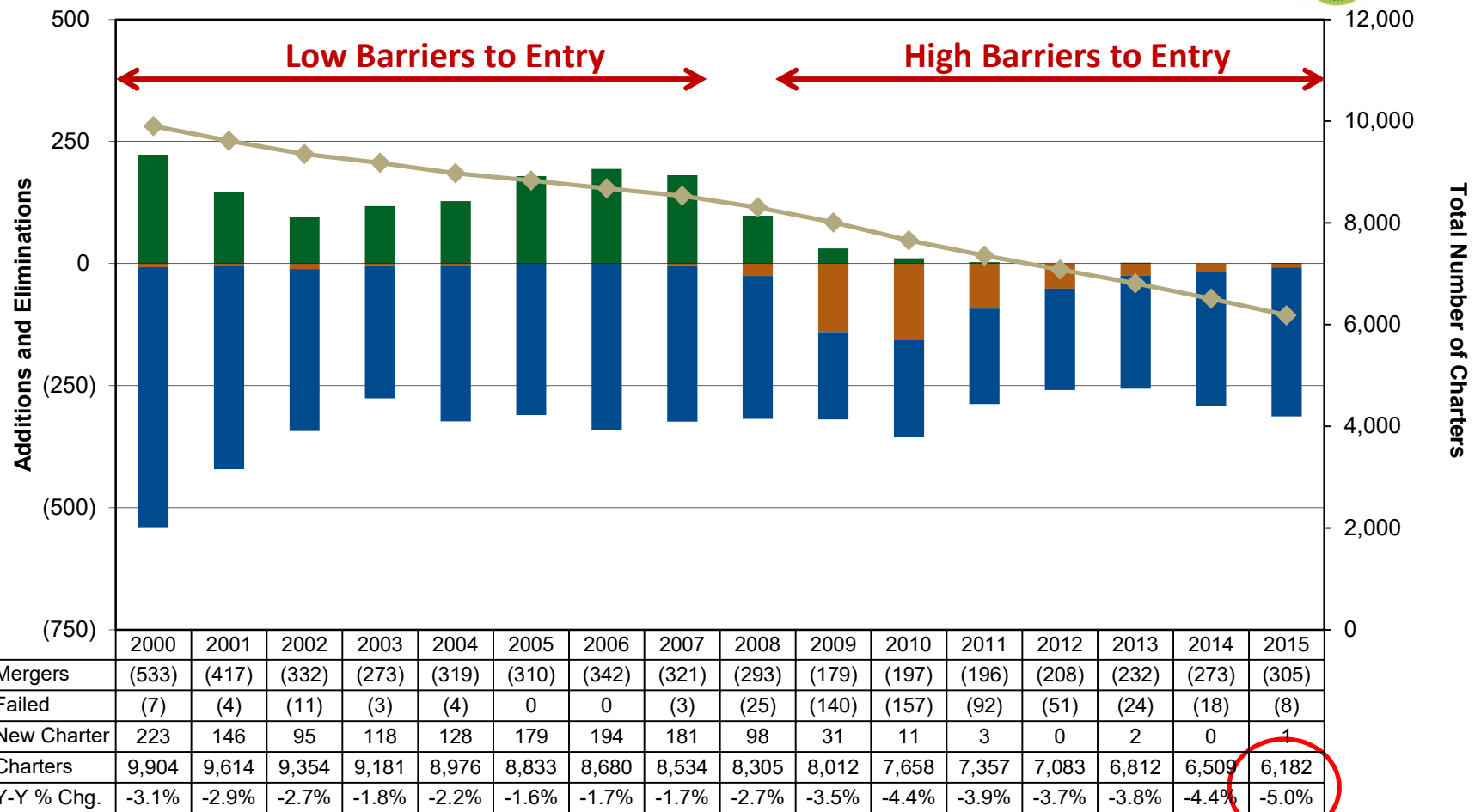


- Industry consolidation
- Increasing regulatory compliance requirements
- Lack of product / service differentiation
- Need for cost savings

21

CONSOLIDATION TRENDS

Since 2000



Source: FDIC.gov

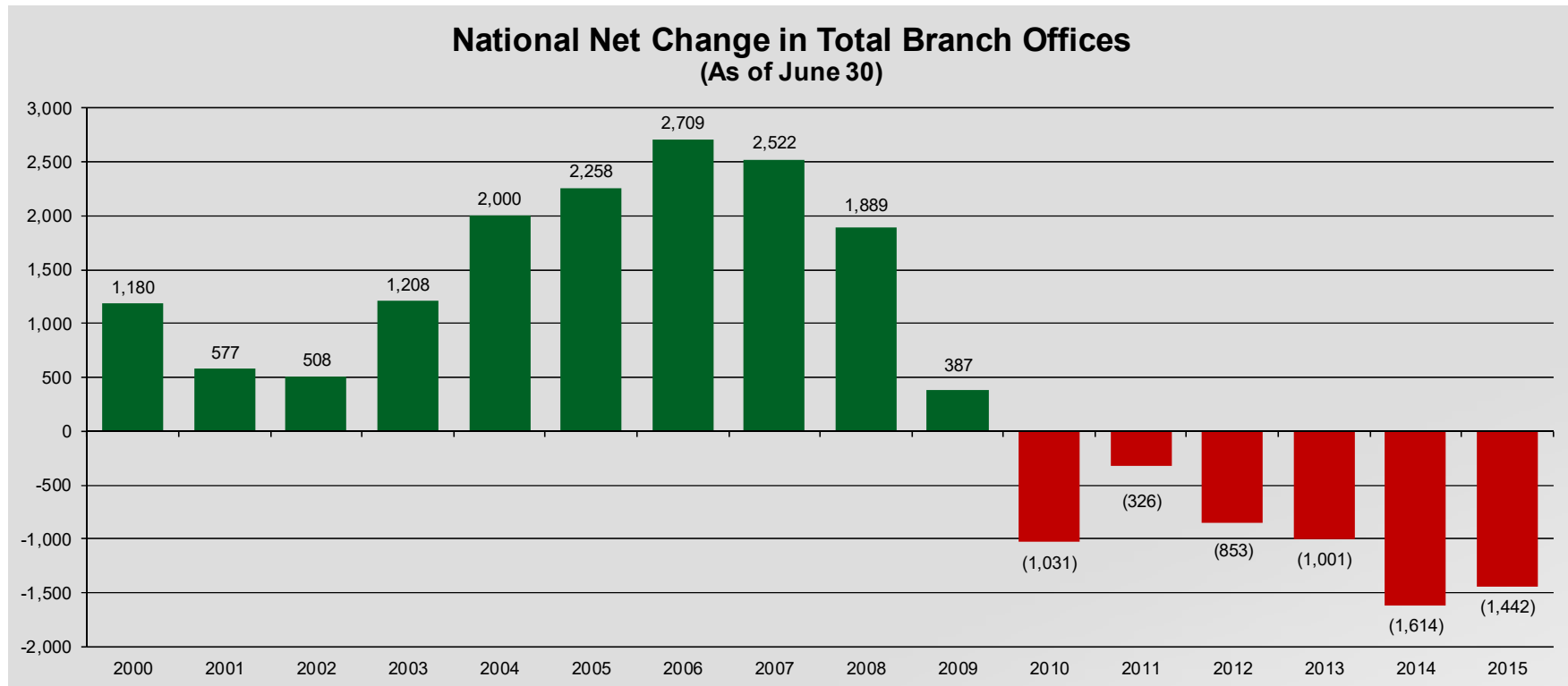


@FMS_Inc #FMSchampion #FMSForum2016

www.fmsinc.org | 800-ASK-4FMS

BRANCHING TRENDS

Net Change in Branches Since 2000



Source: FDIC – Summary of Deposit information.

Branch Transformational Strategies

June 13, 2016



III. The Branch's Impact on Bank Profitability

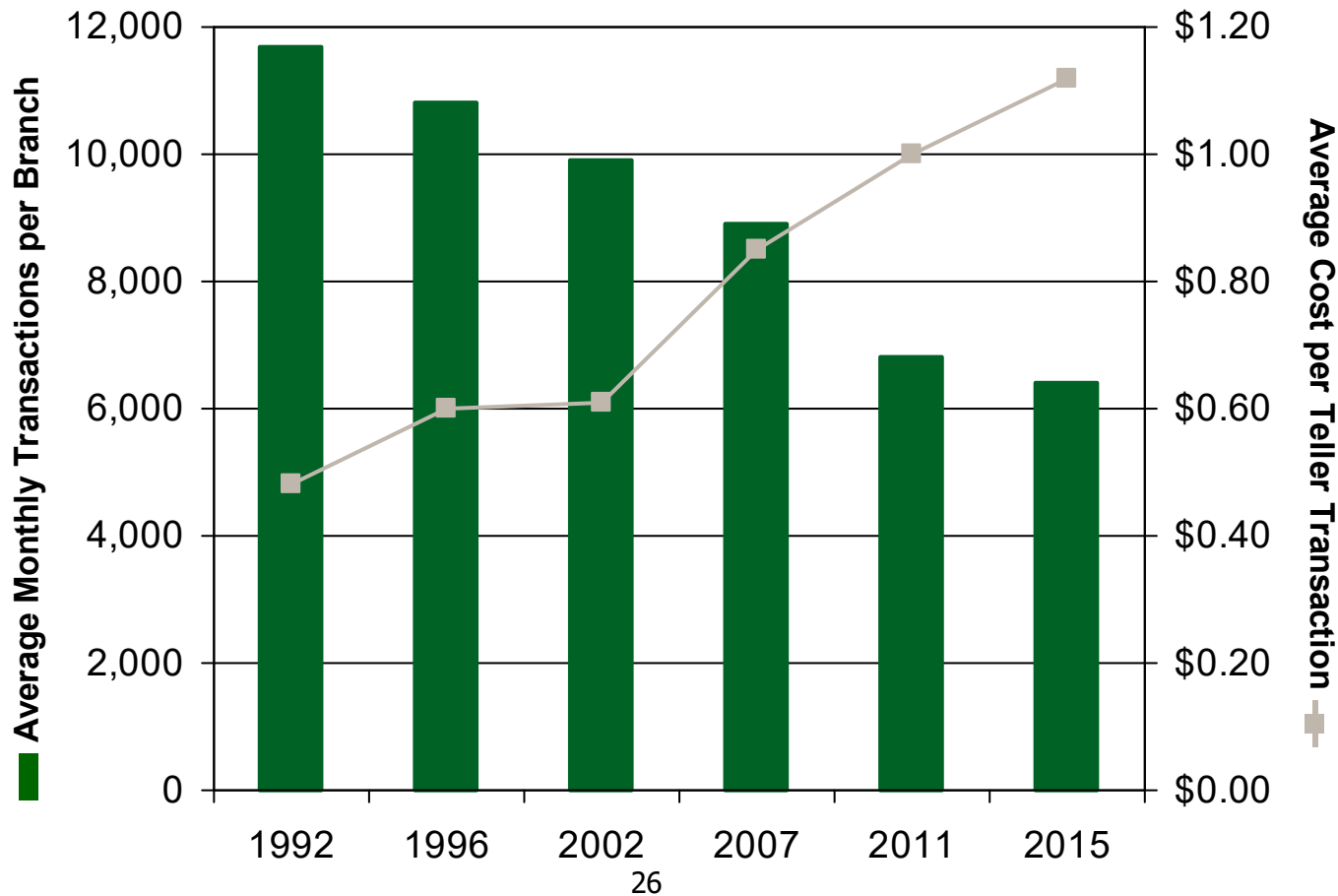
PROBLEMS WITH EXISTING BRANCHES

- Rapidly decreasing transaction volumes
- Decreasing customer visits
- Larger than currently needed
- Overstaffed
- Expensive / costly
- **Not configured with appropriate technology**

25

BRANCHING TRENDS

Since 1992: Cost per transaction has doubled
Monthly branch volume is half

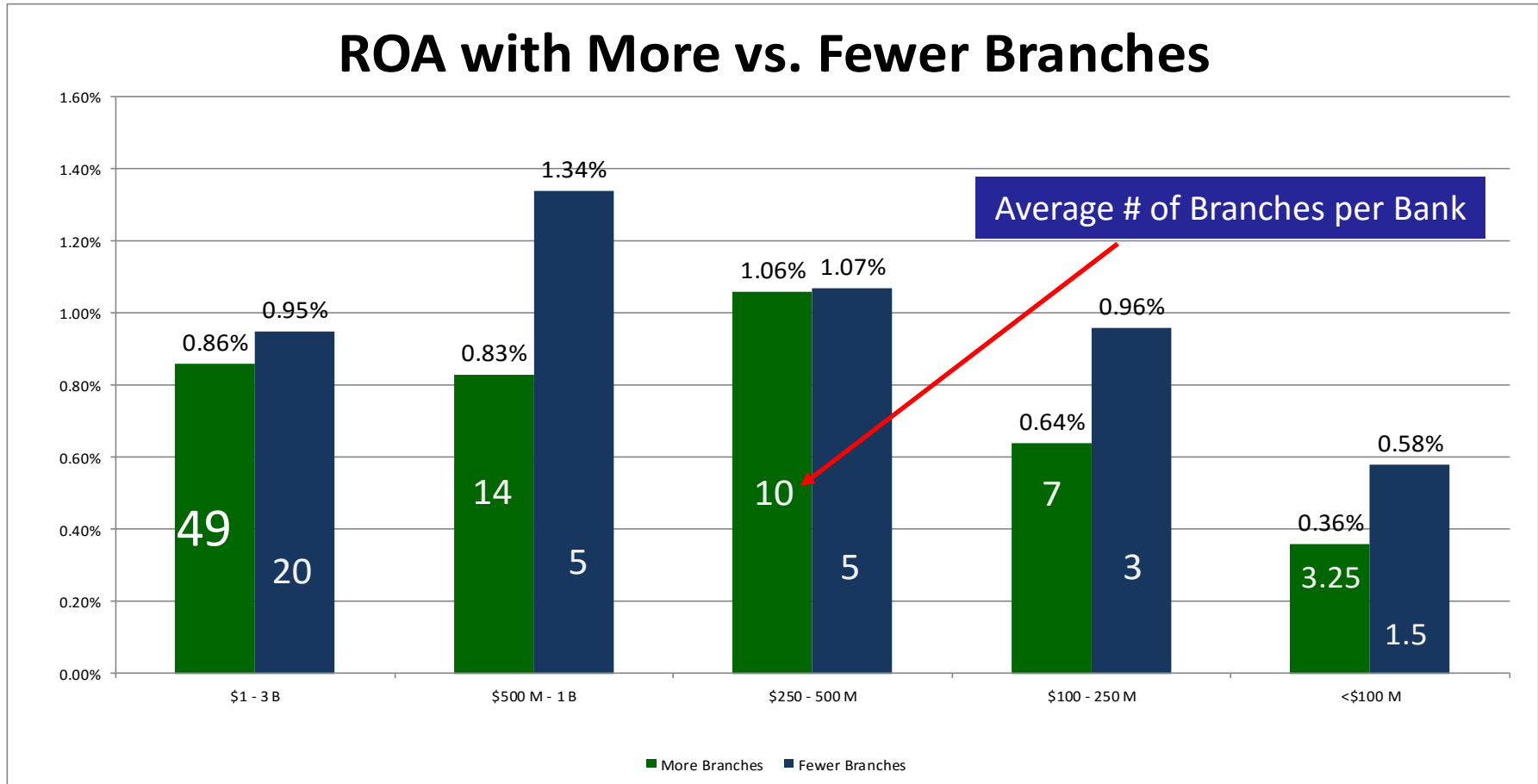


Source: 2015 FMSI Teller Line Study – May 2015

ARE BANKS WITH FEWER BRANCHES MORE PROFITABLE THAN BANKS WITH MORE BRANCHES?



ROA with More vs. Fewer Branches



27

MORE INDUSTRY TRENDS



- Penetration rate of on-line bill pay in the US is **only** 50%
- 90% of US households live within 10 minutes of 3 different FI's
- 75% live within 10 minutes of 6 or more
- By 2020 – 95% of all banking transactions will take place digitally

28

- McKinsey & Company

HAS YOUR BRANCH NETWORK BECOME A DINOSAUR ?



THE WAY BANKING GETS DONE IS CHANGING...

The Finance & Accounting Forum
For Financial Institutions

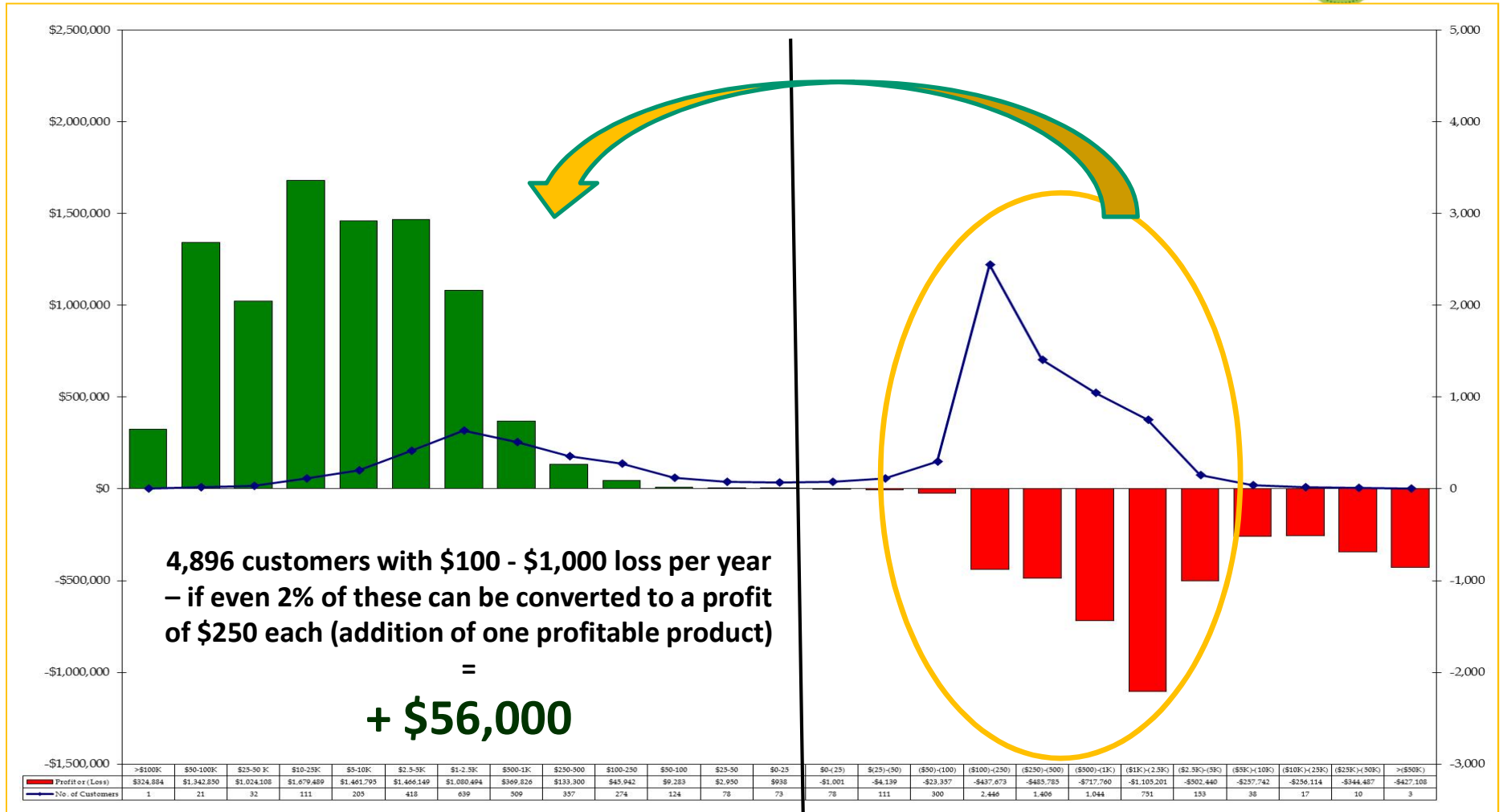
NEW. NOW. NEXT.
NEW ORLEANS



All Self-Service Channels are Growing

CUSTOMER PROFITABILITY

USING BRANCH TRANSFORMATION TO GENERATE IMPROVEMENTS



Branch Closure Testing



Asks the Question...

Would our bank be financially better off without one or more of our current branch facilities?

Starts with Branch Profitability Information

- Net Interest Margin by Branch
- Fee income generated

Exclude standard
cost allocation

32

Branch Closure Testing



Backwards Break-even Analysis

Determine Hard Dollar Cost Savings if Closed \$\$\$



What % of Core Deposits Lost if Closed?

33

Branch Closure Testing



Factors to Consider

- ✓ Distance to next closest branch
- ✓ Prospects for growth
- ✓ Quality and extent of loan referrals
- ✓ Historical trends of growth & profitability
- ✓ Top 50 most profitable customer review

34

Branch Transformational Strategies

June 13, 2016



IV. Do-it-yourself service

SELF-SERVICE BANKING OPTIONS



- Traditional ATM 1969
- Telephone banking 1980
- On-line banking 1994
- On-line bill payment 1995
- Mobile banking 1999
- Remote deposit capture 2003

36

ATTRIBUTES OF VARIOUS SERVICE DELIVERY METHODS

Self Service Channels

(Web Based Banking, Mobile)

- ❖ Convenient
- ❖ Fast
- ❖ Low Cost
- ❖ Preferred by Millennials

Traditional Branch

- ❖ Person to person service
- ❖ Takes time
- ❖ Very High (and rising)
- ❖ Preferred by Baby Boomers

TRANSACTIONS THAT NO LONGER REQUIRE A BRANCH

- Cash Deposit
- Cash Withdrawals
- Credit Card Transfers
- Opening of a deposit account
- Personal loan application
- Credit card application

38

TRANSACTIONS THAT STILL REQUIRE A BRANCH



- Business loans (Branch or LPO)
- Investment advice (In person)
- Problem resolution
- Portions of mortgage loan application process
- Retirement planning assistance (In person)

39

Branch Transformational Strategies

June 13, 2016

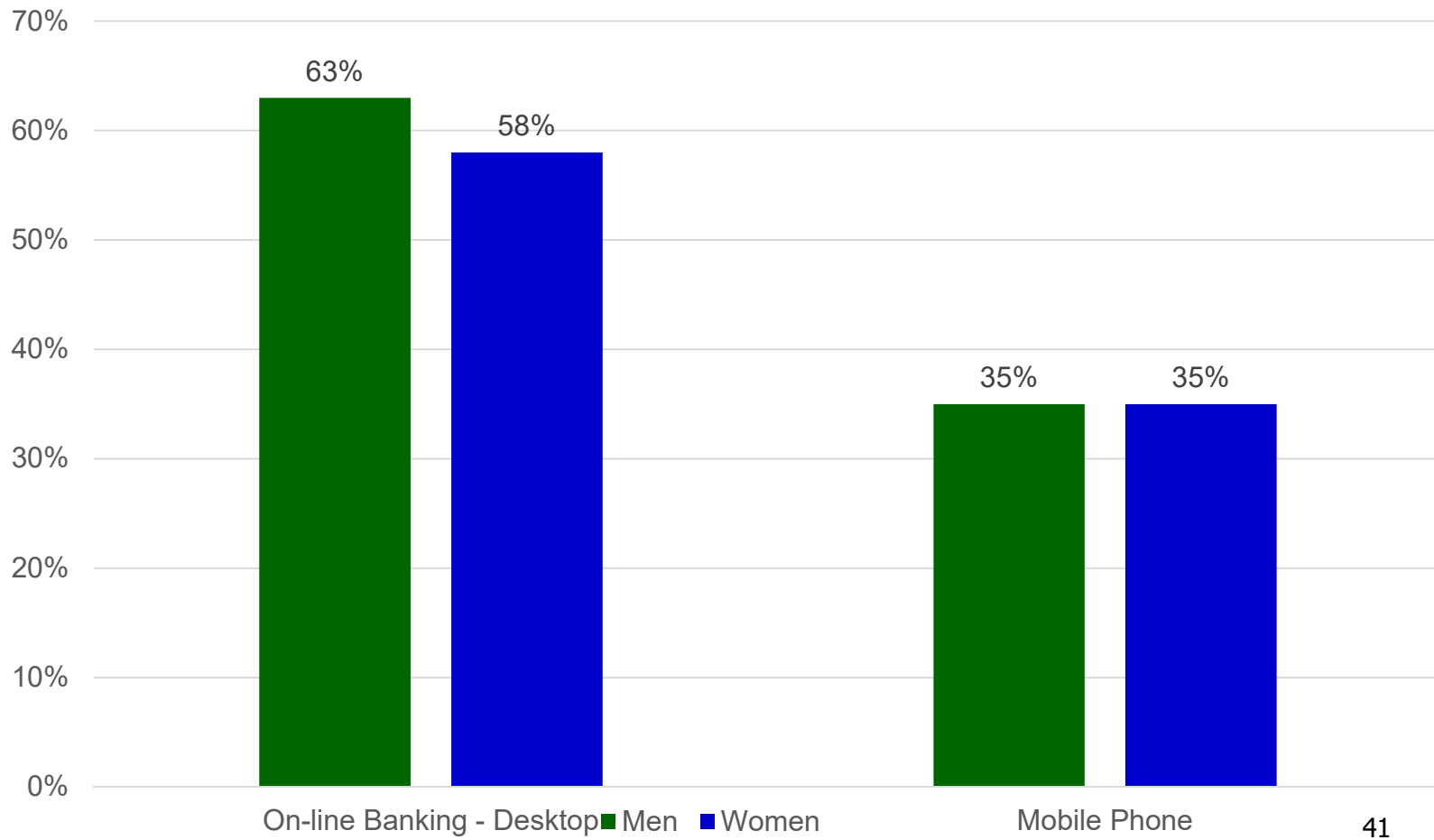


V. Today (and tomorrow's) customer

WHO IS TODAY'S CUSTOMER?



Technology Use by Demographic Group - GENDER



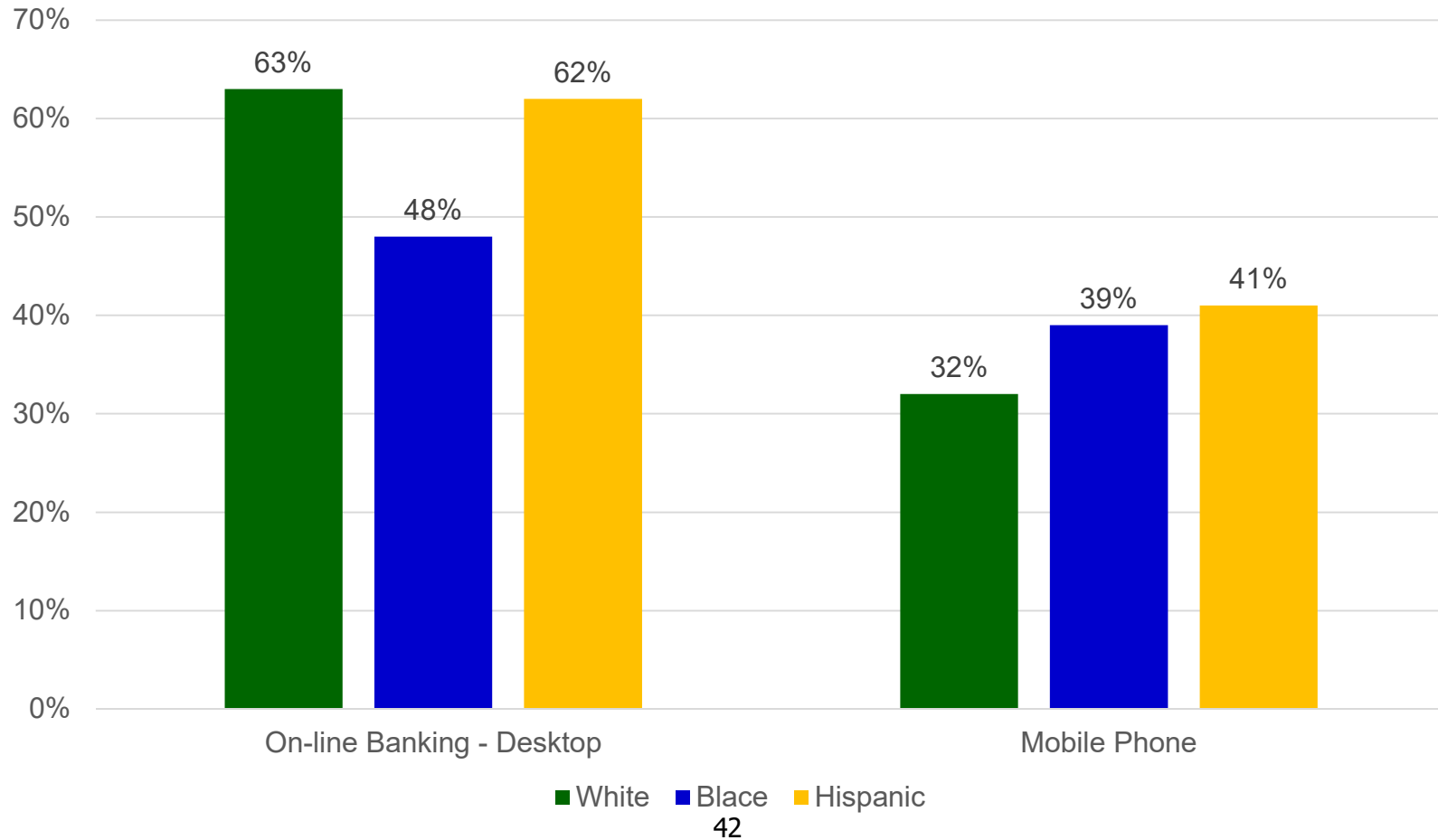
- Pew Research



WHO IS TODAY'S CUSTOMER?



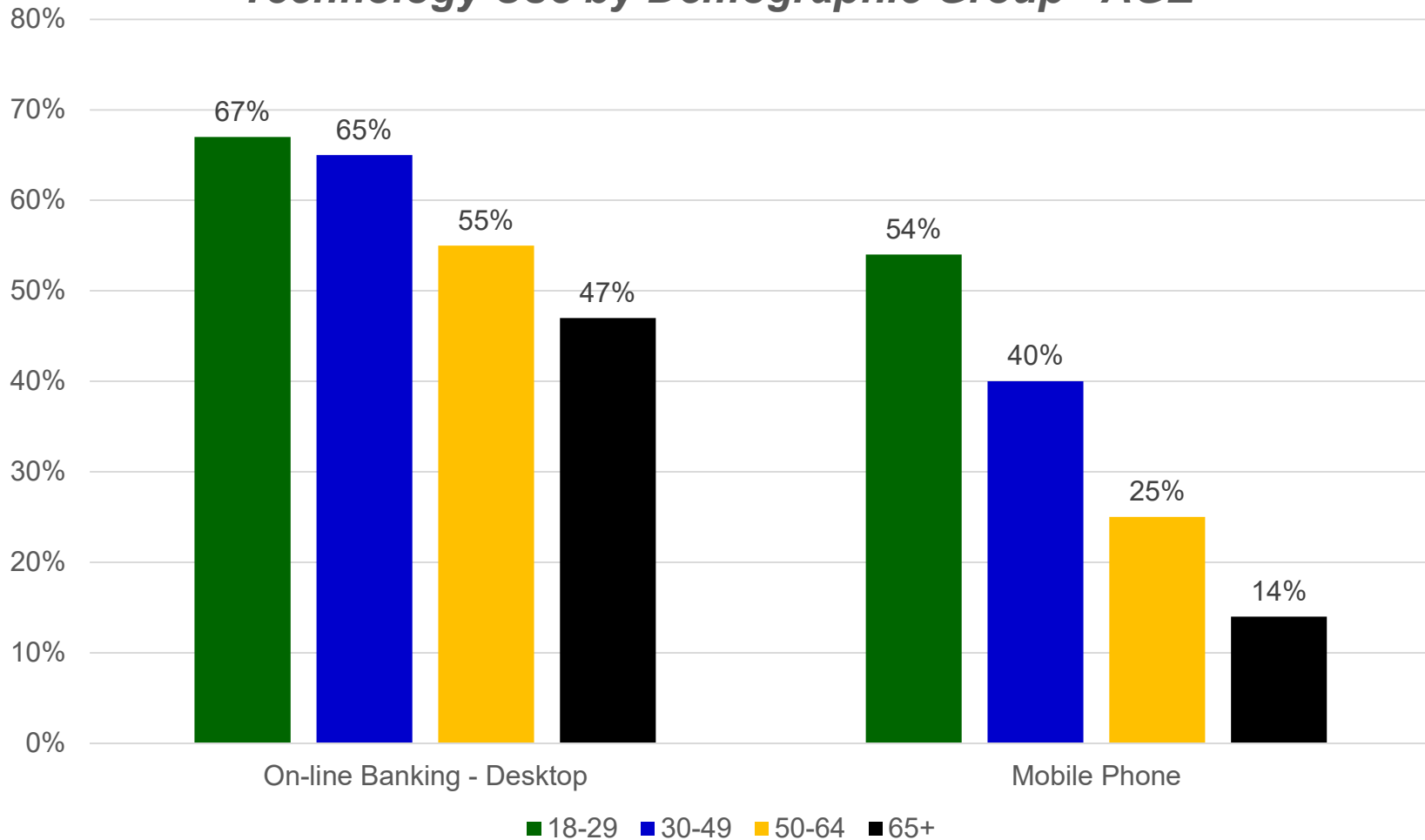
Technology Use by Demographic Group - ETHNICITY



WHO IS TODAY'S CUSTOMER?

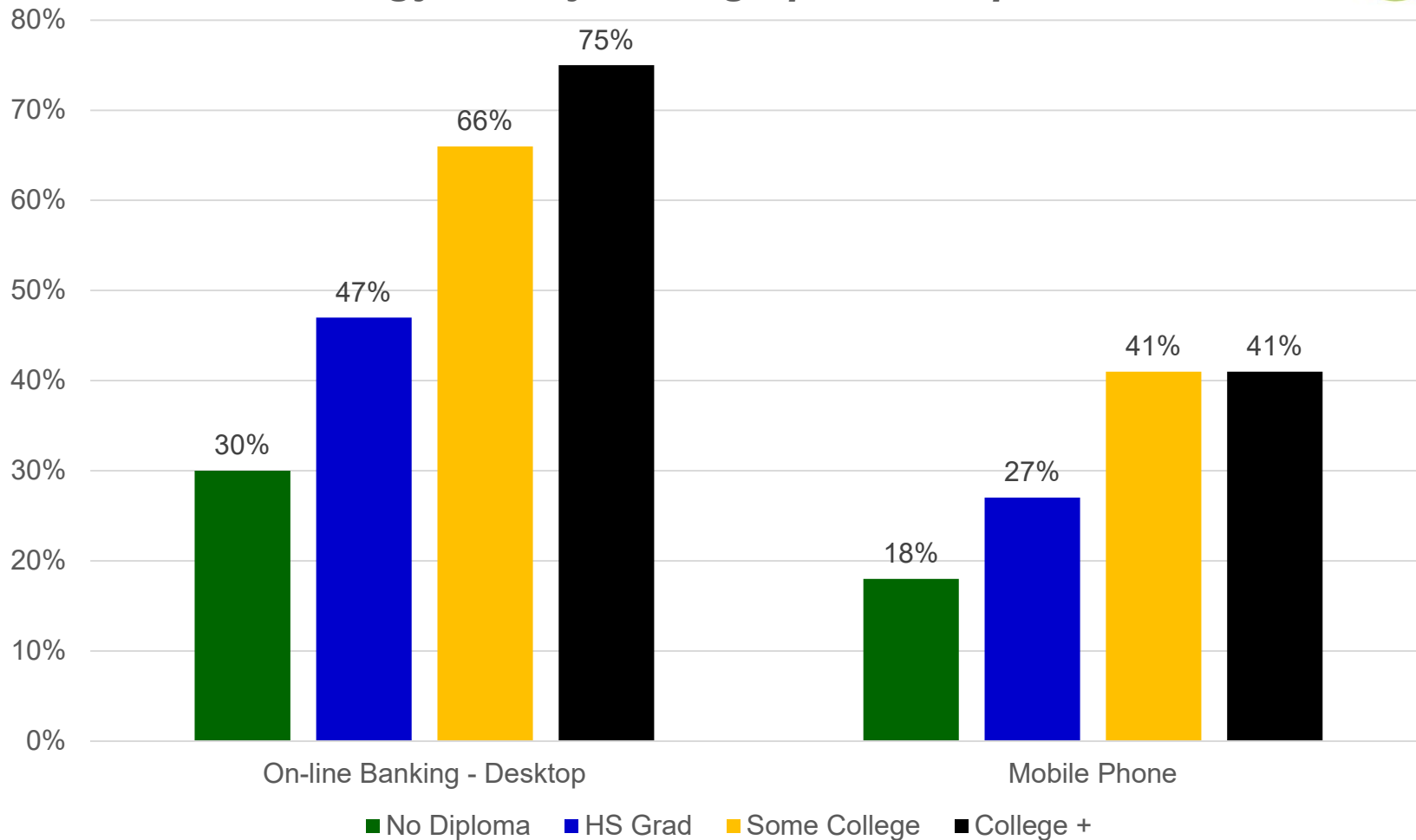


Technology Use by Demographic Group - AGE



WHO IS TODAY'S CUSTOMER?

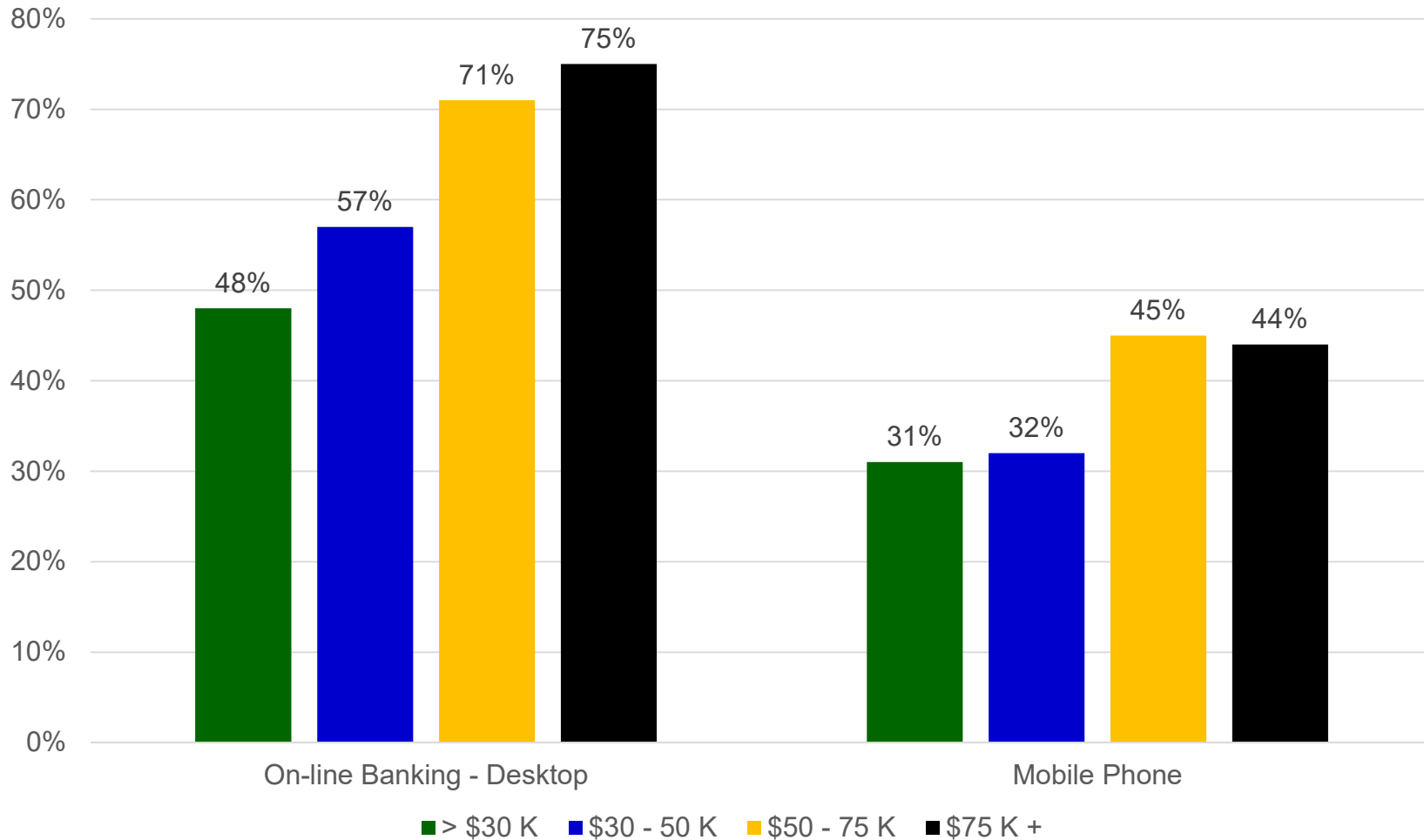
Technology Use by Demographic Group - EDUCATION



WHO IS TODAY'S CUSTOMER?



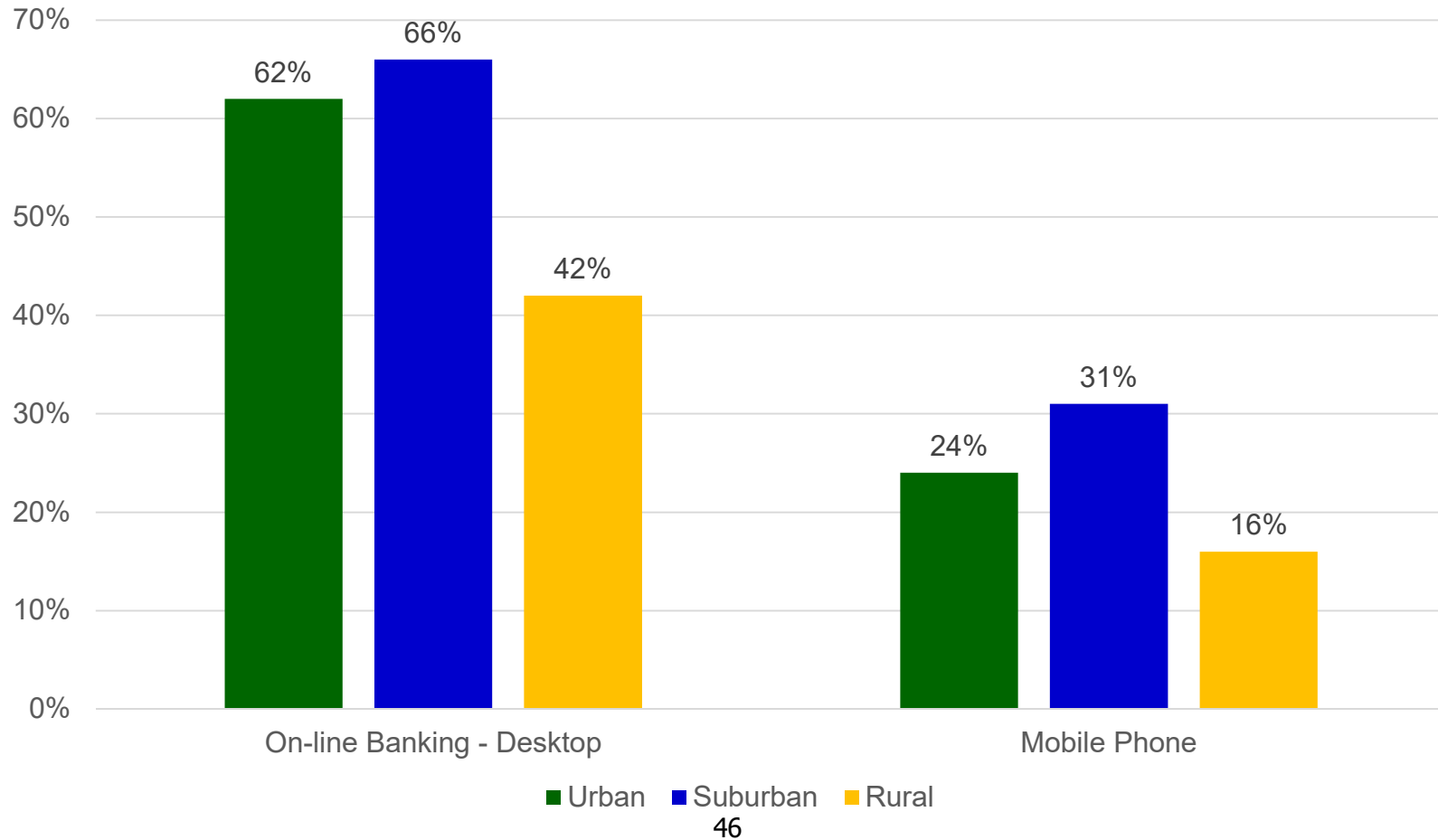
Technology Use by Demographic Group - INCOME



WHO IS TODAY'S CUSTOMER?



Technology Use by Demographic Group - DWELLING



TODAY (AND TOMORROW'S) CUSTOMER



Demographic categories to watch

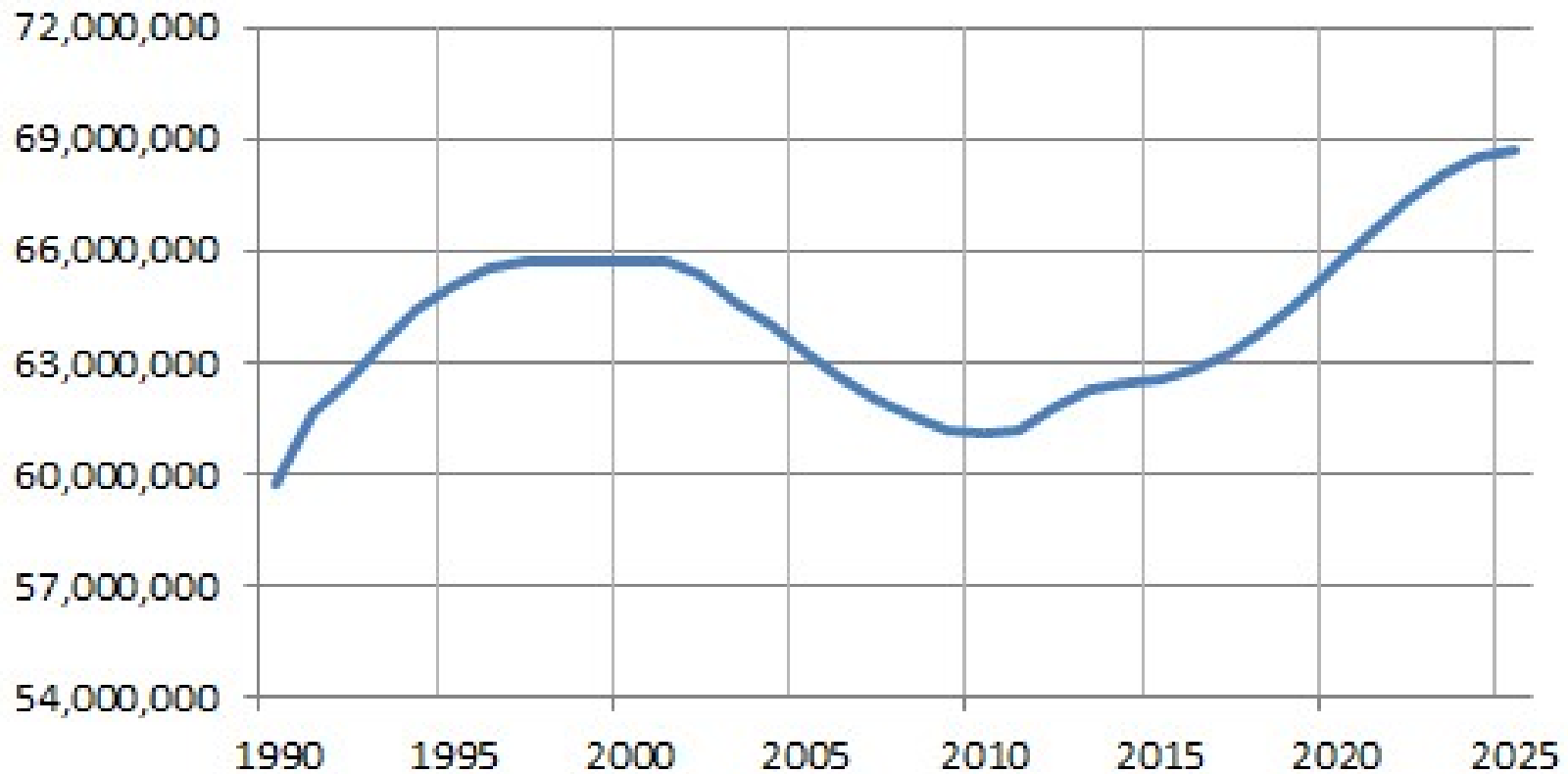
- **Age** is by far the most important at this point in time
- Followed by **ethnicity** (growth in Hispanics and Asians, foremost)
- **Gender**
- **Income**
- **Educational Level**

47

TODAY (AND TOMORROW'S) CUSTOMER



U.S. population, age 30-44



TODAY (AND TOMORROW'S) CUSTOMER



Why is the growth in 30 – 44 year olds so important?

- This age group # 1 in new business formation
 - Most new jobs comes from businesses < 5 years old
- They buy a lot of homes
- They also buy a lot of new cars

- This age group is a major driver of the US Economy

49

TODAY (AND TOMORROW'S) CUSTOMER



The impact of Millennials

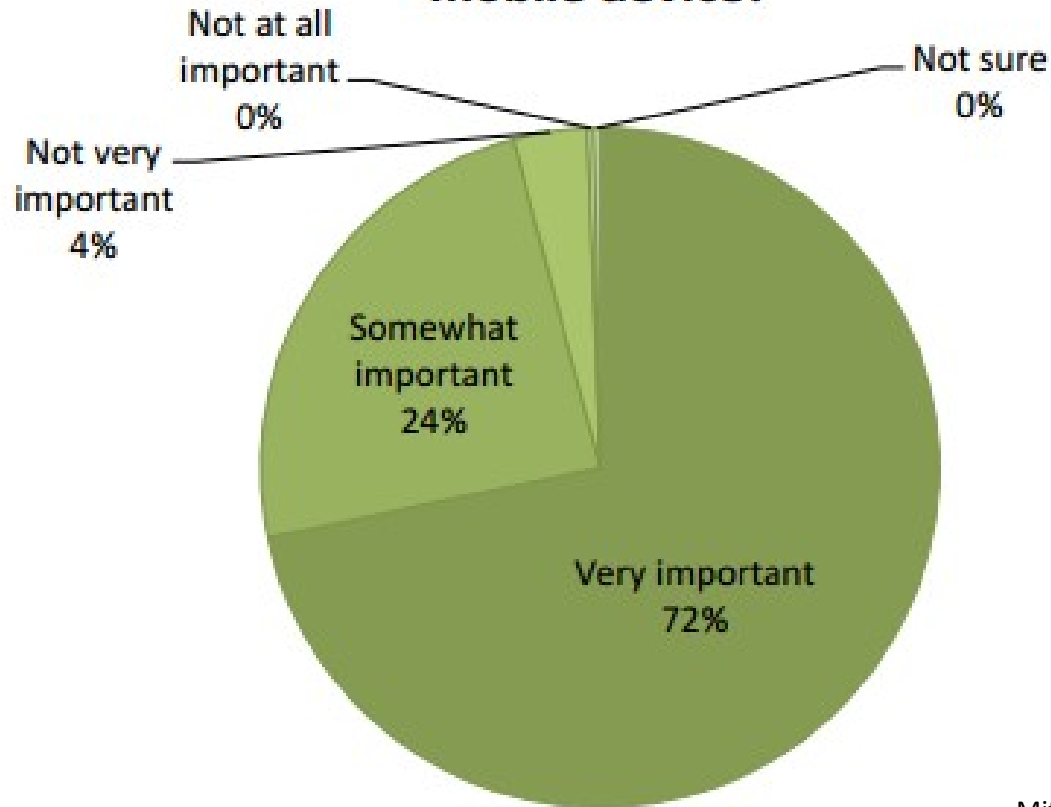
- 86% of this group owned a smart phone in 2014
- Desire to do everything on their mobile devices
- Next, they want to digitize all commerce through their mobile camera
- 86% make purchases with smartphone (11% every day)



50

TODAY (AND TOMORROW'S) CUSTOMER

How important to you is the camera function of your mobile device?



- Mitek, eMarketer

TODAY (AND TOMORROW'S) CUSTOMER



The impact of Millennials

- 42% will switch companies based on mobile apps
- 54% report making mobile deposits with smartphone cameras
- 51% have a mobile wallet
- 86% willing to take extra steps for security

- Zogby Analytics

52

I AM SOOOO NOT ADDICTED
TO MY SMARTPHONE, BECAUSE
I HAVE AN APP THAT WARNS ME
IF I'M TURNING INTO AN ADDICT
AND IT HASN'T GONE OFF YET.



Branch Transformational Strategies

June 13, 2016



VI. Transformational Strategies

NEED FOR TRANSFORMATION



Powerful forces are reshaping the banking industry. Customer expectations, **technological** capabilities, regulatory requirements, **demographics** and economics are together creating an imperative to change.

Banks need to get ahead of these challenges and **retool** to win in the next era. Banks must not only execute on today's imperatives, but also radically innovate and transform themselves for the future.

- PWC Study on banking in 2020

55

THE PURPOSE OF THE BRANCH

- Branch vs. Sales Office
- Service vs. Sales
- Growth within stagnant markets

What is the cross-selling effectiveness of branch staff vs your on-line or mobile banking app?

NECESSARY CONDITIONS TO SUCCEED

- Right people right place
- Effective incentives

56

THE FUNCTIONS OF THE BRANCH



- Represents & projects the organizations **BRAND** to the community
- Provides a physical presence
- **Serves the FULL range of customer needs**
- The heart of the bank's franchise
- A source for revenue generation
- **New business development**

57

BRANCH MANAGERS ROLE



Traditional

- Lead, motivate & engage the team
- Build & increase customer loyalty
- Mitigate risks through compliance
- Accomplish retail banking goals

Future

- Balancing usage by channel

58

GOALS FOR THE BRANCH



- **Increase sales**
- **Service Quality**
- **Decrease risk**
- **Reduce costs**

59



TRANSFORMATION



FROM

BRANCH BASED CUSTOMER RELATIONSHIPS

TO

MULTI-CHANNEL NETWORKS BASED ON TECHNOLOGY WHICH INCORPORATES THE BRANCH AS SIMPLY ONE CHANNEL

MAJOR CHALLENGE

IT WILL BE ESSENTIAL THAT THE NEW MULTI-CHANNEL NETWORK BE MORE EFFICIENT THAN THE BRANCH ONLY NETWORK THAT PRECEDED

60

BRANCH PROFITABILITY ENHANCEMENT

More recent efforts

- Provide in branch self service options
- Push mobile
- Push on-line banking
- Call center / virtual branch
- Remote teller networks
- Push remote self service options
- Use of CRM to leverage customer knowledge

Traditional efforts

- Reduce hours
- Cut staff
- Smaller offices
- Push ATM use
- Bank by phone
- Close Branches
- Remote deposit
- Import work from other locations

61

TRANSFORMATION



ESSENTIALLY ALL ROUTINE TRANSACTIONS PUSHED TO ELECTRONIC CHANNELS

FACE TO FACE MEETINGS BECOME ALL ABOUT SALES / ADVICE

62

BRANCH TRANSFORMATION GOALS



“.....optimizing the channel mix as a part of a multi-channel strategy.....”

“.....responding effectively to the changes in consumer behavior....”

63

RESPONSES TO CHANGING ENVIRONMENT



- Changes in number, size & location of branches
- Increased use of automation
- Greater use of specialist staff
- Private offices – not teller lines (personal advisory services, not transactions)
- Non-staffed (fully automated) branches
- Use of remote advisors

64

BRANCH TRANSFORMATION IMPACTS



Estimated impact on efficiency ratio for a typical retail bank (efficiency ratio declines as it improves), percentage points

Opportunity

Migrate teller deposit and withdrawal transactions to digital channels

Migrate teller payments and services to digital channels

Increase use of online bill pay

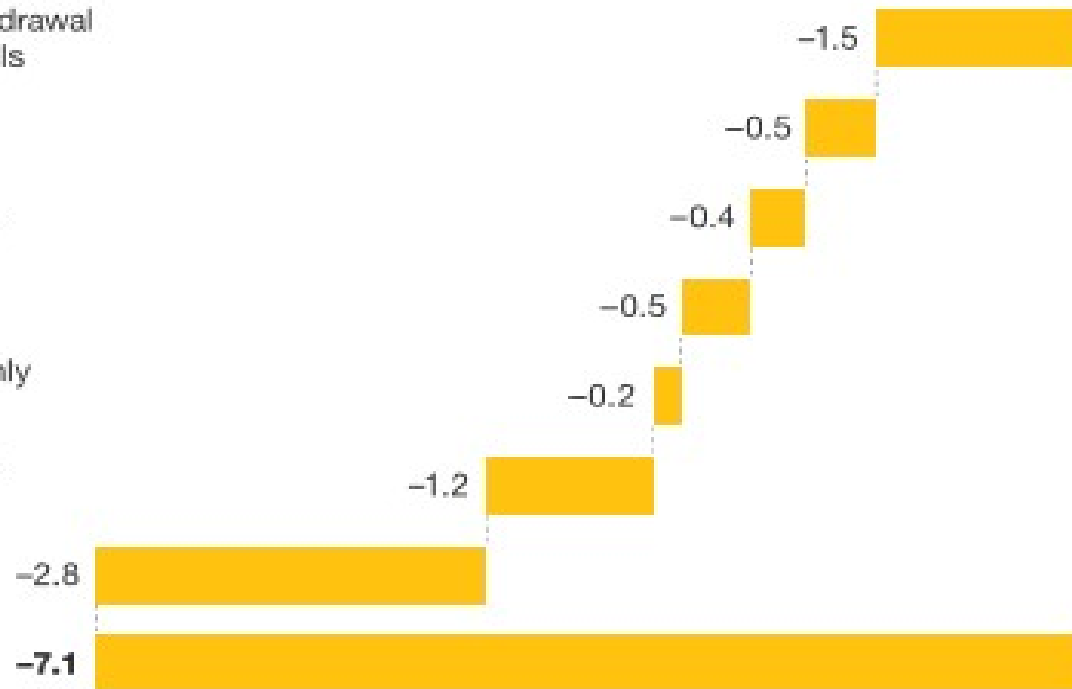
Increase use of debit cards

Increase adoption of online-only statements

Introduce new branch formats with smaller footprints

Thin the branch network

Total opportunity



65

CHANGES IN BRANCH ASSOCIATE EXPERTISE



- More advisory in nature
- Importance of selling over service
- Greater need for education and training
- **You can't transform the Branch without transforming the Branch Staff**

66

A serious question for you to contemplate...?



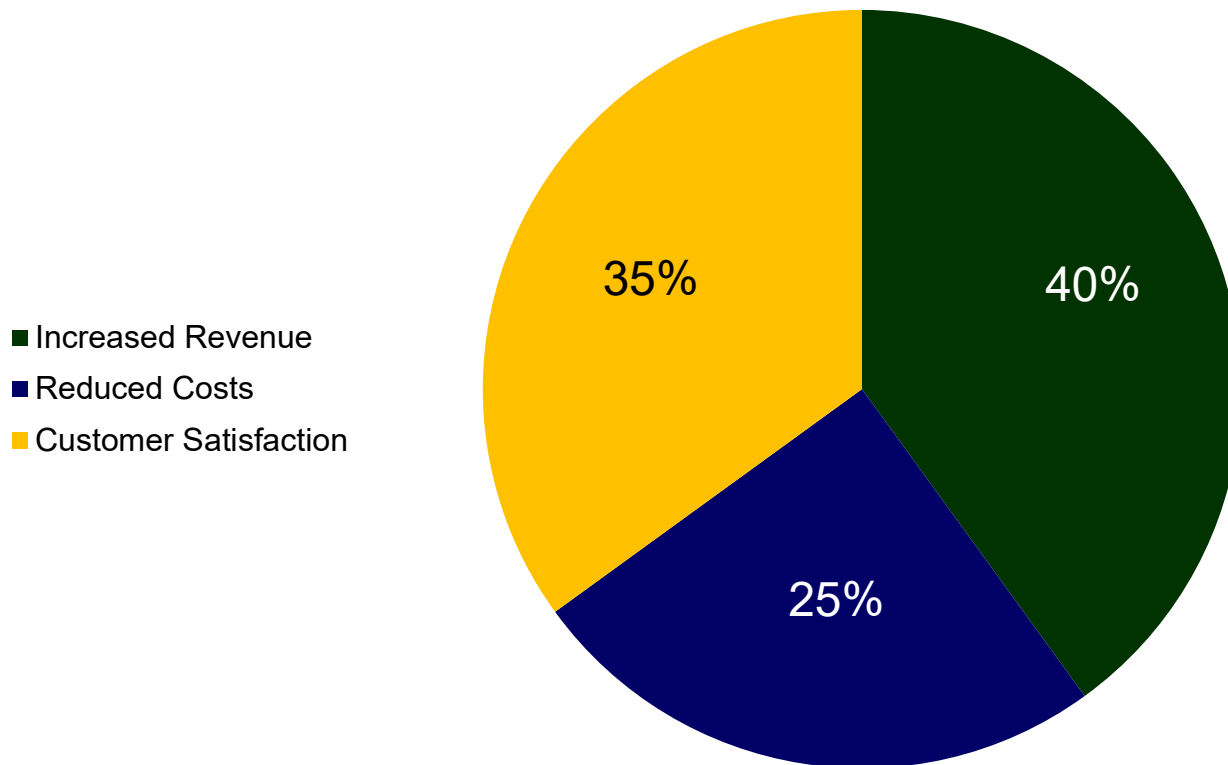
As community banker's, it is sometimes difficult to clearly differentiate our unique bank service offerings from those of the bank down the street.

If we are offering the same mobile banking app, bill payment and on-line banking solution as do most other community banks, how do we expect our customer's to recognize our bank's unique differences?

PAYBACK ON BRANCH TRANSFORMATION



Sources of Payback

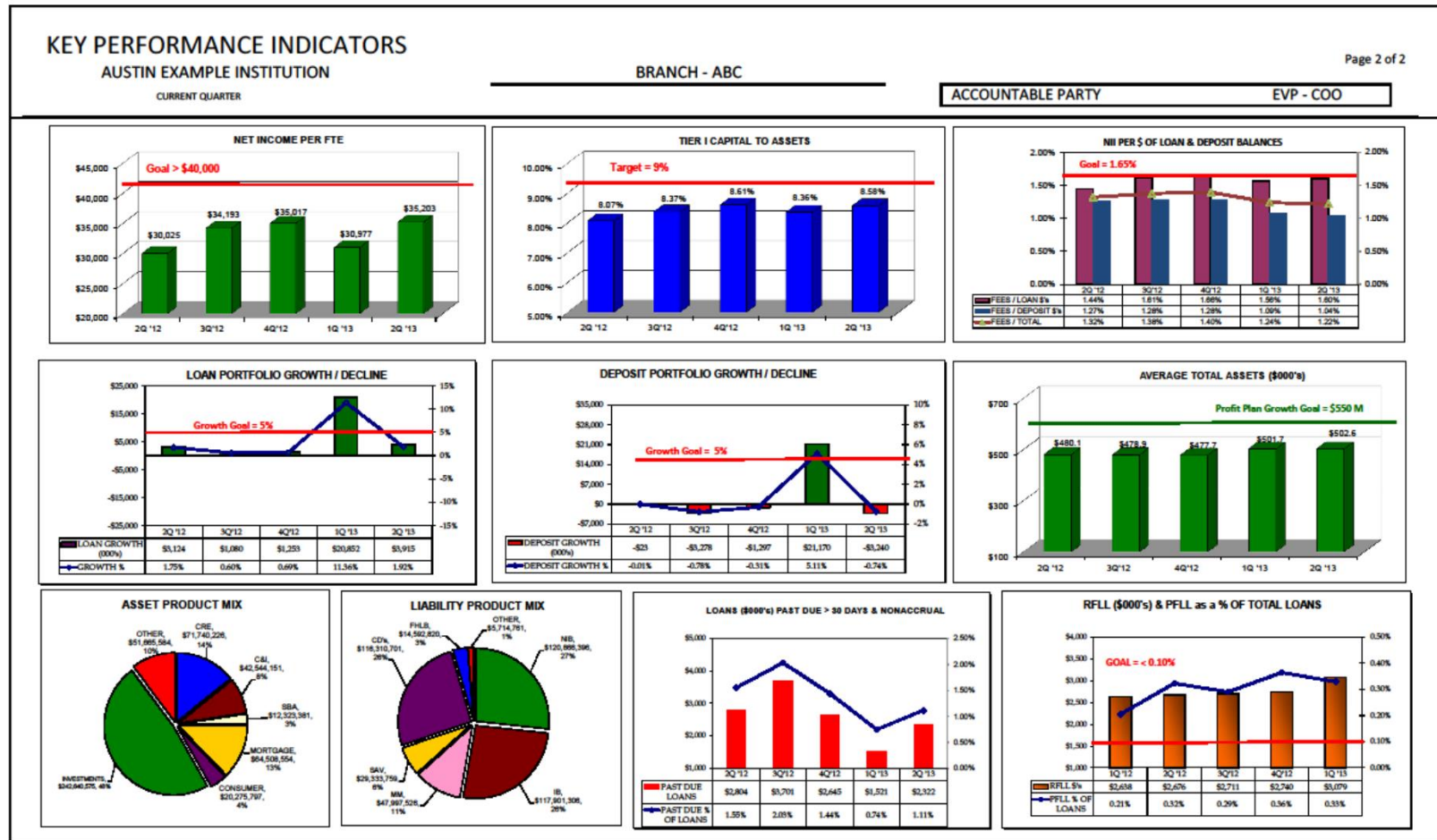


- Increased Revenue
- Reduced Costs
- Customer Satisfaction

McKinsey & Company, August, 2014

68

DASHBOARDS TO MONITOR PROGRESS



NEW METRICS



- Channel Profitability
 - Volume
 - Cost
 - Revenue
- Proportional use by Customer of each channel

70

Time for a few questions ?



**THANK YOU FOR ATTENDING TODAY'S
PRESENTATION!**

71



PRESENTER

Jeff Morris- joined Austin Associates' Financial Management Division in 1998. He is responsible for profitability analysis services and works with clients who utilize the firm's innovative software products, including its proprietary organization/product/customer profitability software and its loan and deposit pricing software, with over 35 years experience in various financial management roles.



Jeff Morris

Managing Director & Principal
Financial Management & Consulting

jmorris@austinassociates.com

419-517-1775

72

AUSTIN ASSOCIATES, LLC

Financial Management Consultants for Community Bankers

- Community bank advisors for more than 40 years
- Specialized consulting and advisory services
 - Asset / Liability Management
 - **Profitability Measurement & Improvement**
 - Loan & Relationship Pricing Systems
 - Balance Sheet Structuring
 - Regulatory Compliance
- Current owners are consultants/managers
- Over 200 bank/thrift clients in 2014 in 26 states

73

CONTACTS

We appreciate hearing from you.

If you have questions or comments, regarding today's presentation, or if you would like to discuss your branch and channel network transformation plans, please feel free to contact us at any time.

We would also be pleased to provide your management team with a personalized demonstration of the Austin Profitability System - simply contact Jeff to arrange a date and time for your demo.

Jeff Morris

**Managing Director & Principal
Financial Management & Consulting**

jmorris@austinassociates.com

419-517-1775

74