

Branch Sales – Opportunity Based Myths

Common Misconceptions of Branch Sales Performance

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FINANCIAL SERVICES

Brian Diepold • PhD, Senior Client Services Manager, Pitney Bowes Business Insight



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ABSTRACT

WITH THE ANNUAL BRANCH GOAL SETTING SEASON COMING TO AN END, BUT CERTAINLY NOT OUT OF MIND, IT SEEMS TIMELY TO DISCUSS SOME MISCONCEPTIONS ABOUT BRANCH OPPORTUNITY. GIVEN THE ECONOMIC CLIMATE, BANKS ARE RETURNING THEIR ATTENTION TO MAXIMIZING THE PERFORMANCE OF EXISTING BRANCH NETWORKS, RATHER THAN BUILDING NEW.

THIS RESEARCH PROVIDES INSIGHT INTO KEY FEATURES OF OPPORTUNITY-BASED GOAL SETTING AND SHEDS LIGHT ON A FEW COMMON MISCONCEPTIONS OF BRANCH SALES PERFORMANCE. THIS PITNEY BOWES BUSINESS INSIGHT WHITE PAPER INTRODUCES KEY MODELING FEATURES WHILE ADDRESSING COMMON QUESTIONS AND CONCERNS SURROUNDING THE GOAL SETTING PROCESS.

ESTABLISH BRANCH SALES GOALS BASED ON THE ATTAINABLE NET GROWTH OPPORTUNITY FOR EACH BRANCH ACROSS ALL PRODUCTS

Understanding Opportunity

Given the economic climate, banks are turning their attention to maximizing the performance of their existing branch network, rather than building new. While this is not a universal truth, it is certainly true for most banks these days. The branch boom is over, and the easiest way to acquire new customers – build a new branch – is simply not as popular or economically responsible as it was a decade ago. This is a world where banks can benefit from closely managing the performance of existing cost centers and, as a result, opportunity-based goal setting seems to be a hot topic, once again.

While the process of annual branch goal setting takes up only part of the year for most, it is certainly never far from anyone's mind. Reflecting on the process reveals some common misconceptions about branch opportunity.

More to the point, what is the right way to measure that opportunity?

An insightful way to answer that question is to unravel some conventional wisdom around branch sales. As this paper works through some myths of branch sales, the answer to that question will become apparent. By measuring and understanding branch performance and market circumstances in a consistent and objective manner, banks can position themselves to establish branch sales goals based on the attainable net growth opportunity for each branch across all products.

Reflecting a bit on past goal setting seasons, there are five myths of branch sales that will certainly shed some light on the topic.

Myth #1

Big Goals Punish High Performing Branches

When assessing opportunity, it is common to start with the principle that top performers should not continue to be punished. This is an outstanding principle, but the hard part is digging into how large or small the goal needs to be to achieve this principle. Consider the example of branches with large existing books of business. These branches often have reached this point by selling large volumes of accounts year after year. The most common concern among sales managers during goal setting season is that the goals for next year will ask too much of branches that have already contributed large sales in the past.

But, this myth is not quite correct. Determining whether a branch is being punished, otherwise known as setting a big goal, comes down to how a big goal is defined. Yes, it is true that high performing branches will be asked to contribute more than their share if goaled for large net growth. In fact, there are two key words in that sentence – if and net. Large successful branches often sell high gross volumes of accounts without much net growth. The principal reason is that these branches have a much larger base of households from which to cross-sell. This is certainly a part of the branch opportunity that is captured in sales performance.

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Figure 1 shows annual gross branch sales of checking accounts over the beginning book of business for checking accounts for a sample of branches. This highlights the perception that large and successful branches continually sell larger volumes of accounts.

Figure 2 shows annual gross branch sales of checking accounts over the number of attrited accounts. A very similar relationship holds here as was true in Figure 1. That is, large branches attrite more accounts, thereby selling more accounts.

Of course, these two graphs do not represent the whole story. If that were the case, then why would any bank need to build a model to measure opportunity? Variation, which is defined by individual circumstances for each location, exists around the relationship for both correlations. This variation is just as important for opportunity-based goal setting as understanding the fundamental relationship between past performance and annual sales.

Truth #1 – Focusing the discussion on net growth opportunity leads to a more accurate and productive conversation about branch sales goals.

Myth # 2 The Best Branches Sell Everything Well

It is commonly thought that the best branches, or the best branch managers, are effectively selling every product, year over year. This is another misconception that can be cleared up by focusing on the right metric – net growth. If branches are being managed by attempting to optimize net growth of the bank, then the focus must shift to growth when trying to understand performance and opportunity. When branch growth is broken down into the growth of individual products, it becomes apparent that certain product combinations have negatively correlated growth rates.

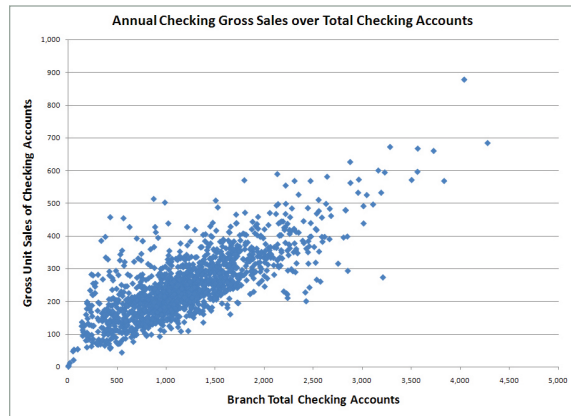


Figure 1: Larger branches sell more

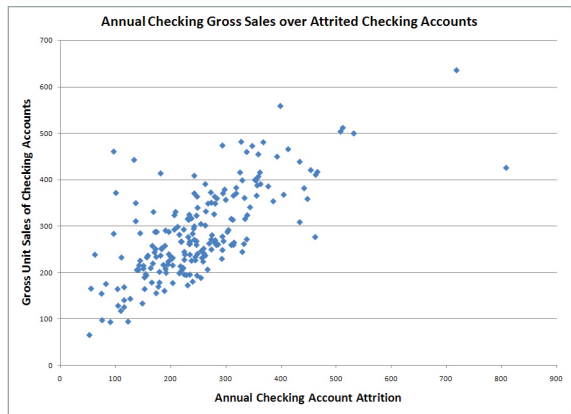


Figure 2: Branches that attrite more, sell more

COMPETITION IS ONE OF THE MOST IMPORTANT VARIABLES IN UNDERSTANDING BRANCH PERFORMANCE AND SALES OPPORTUNITY

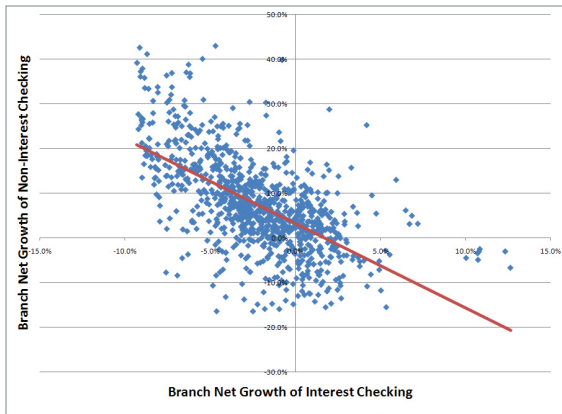


Figure 3: Growth in checking – interest versus non-interest

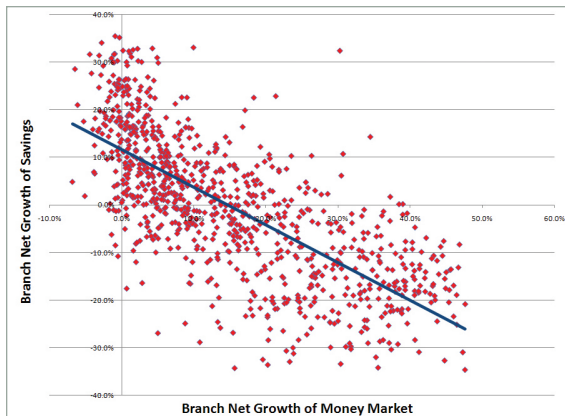


Figure 4: Growth in savings versus money market accounts

Figure 3 shows the annual change in non-interest checking accounts and interest checking accounts for a sample of approximately 5,000 branches.

Similarly, Figure 4 shows the annual change in savings and money market accounts for the same sample of branches.

The evidence suggests that branches growing in one of the product pairs are not able to grow in the other. This indicates that branches simply are not selling everything well. This finding provides reason to believe that opportunity for branch growth is truly product specific.

Truth #2 – The result of appropriate goal setting is to end up with branches that have varying net growth targets across the product suite.

Myth #3 Branch Sales Staff Can Influence Average Account Balances

While not quite as common, an implicit belief that branches can influence the average balance of the accounts they sell, exists in the incentives at many banks. This belief is seen when account and balance goals are set for the same products – or even for a subset of overlapping products. It is important to erase this belief, as the sales staff is going to work towards incentive, and the goal should be logical and attainable. With that in mind, the answer here is that branches have little control over the average balances of the accounts they acquire.

The data shows a tight correlation between average balances of a branch's book of business, and the average balances for that product in the trade area. In other words, the accounts held at any one branch tend to mirror the balances of those accounts in that market, as depicted in

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Figure 5. This shows that while branches may have great influence over the number of accounts they sell, they have far less influence over the balances that are held in those accounts, which is much more market driven.

These findings show that it does not make sense to offer incentives to staff for selling accounts and balances on the same product types. This implicitly incents them to sell accounts with a certain level of average balance, when the data suggests they have little influence over this.

Truth #3 – It is certainly useful to know what balances to expect from a budgeting perspective, but there is very little the branch can do if the unit goal is already consistent with the expected balances.

Myth # 4 Competition Limits the Ability to Sell Any Product

Another common concern during the goal setting process is that a branch is asked to contribute too much given the competition it faces. Typically, this argument is applied to all products – or at least all products where the resulting goal seems high.

Competition is one of the most important variables in understanding branch performance and sales opportunity. But, competition is not a universal truth. Recent research uncovered some interesting specificity around the importance of competition in a market. While it is clear that competition matters for establishing branch goals, it is far more important when measuring opportunity for core deposit products, as opposed to term deposits or loan products.

While the importance of measuring opportunity at the product level is known, and previously discussed in

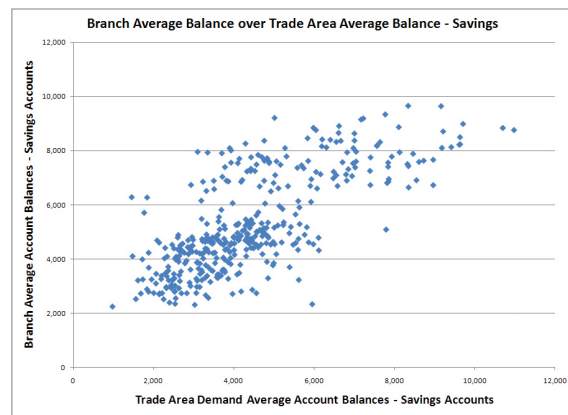


Figure 5: Average balances mirror the market

this paper, this finding supports that notion and adds additional clarity around how to measure that opportunity. The relationship between opportunity and competition is intuitive – the more competition a branch faces, the less likely that branch is to capture a higher market share. But, the relationship is product specific. The impact of competition on acquiring checking customers is much stronger than the impact on acquiring home equity accounts. There is evidence that competition is less important to understanding the opportunity to sell reputation or rate sensitive products. As a result, goal setting needs to account for the variable effects of competition, and account for the bank-specific influence on product sales. For example, if each and every one of a bank's branches are underperforming in a particular product, then it is recognized as a bank specific factor when measuring the opportunity to sell that product at the branch level.

Truth #4 – In the end, it is known that competition is important, but competition cannot be an excuse for a branch not selling a product where the bank has some other comparative advantage.

THERE ARE MANY VARIABLES THAT GO INTO UNDERSTANDING IF A PARTICULAR BRANCH IS MEETING, EXCEEDING, OR UNDERPERFORMING EXPECTATIONS

Myth # 5 **Household Growth is the Most Important Factor in Defining Opportunity**

This fifth and final myth is one that pervades more than just sales goals, and it appears in market analysis more generally. Household growth tends to be an easily accessible and popular metric to define market opportunity. Unfortunately, this is rarely the case, and often times misleading, especially when related to annual branch sales.

It is critical that, when measuring sales opportunities, bankers must go beyond understanding net growth, by also measuring the components of that growth. This mind-set helps to show the amount of gross product that needs to be sold; along with how much can reasonably be attributed to new households or cross-sell to existing households. It is often surprising to learn that demographic household growth, in a market or trade area, contributes very little to the acquisition of new households. The great majority of new household acquisitions are derived from customer churn in the market – or the ability to compete those households away from other banks.

The easiest way to understand this theory is to imagine a fictitious branch trade area. Consider a trade area with ten bank branches and 12,000 households, providing a reasonable 1,200 households per branch. This trade area is expected to experience an annual household growth of 5% – which is a large number for annual demographic growth. The 5% growth in the market leads to 600 new households over the course of the year. By dividing this number across all ten branches, results in 60 households per branch. It is a fairly good bet that every branch in this situation would receive a checking account goal of much greater than 60 accounts. How is this determined? Typically, there is an annual customer churn of approximately 15%. Taking a safe assumption of 12% in the example trade area, that creates an additional 1,440 available accounts across the ten banks

competing for those accounts. In this case, churn alone creates opportunity for about 144 accounts per branch in the trade area – much greater than the 60 accounts from household growth.

The example purposely chose an extremely high annual household growth rate to highlight how important it is to focus on other measures of opportunity. Understanding whether a branch is acquiring its expected share of those 12,000 households is much more important than knowing the demographic household growth rate. If a branch is already capturing more households than expected, it can be concluded that it will be a considerable challenge for that branch to continue to grow its share of households in that market.

Truth #5 – The great majority of new household acquisitions are derived from customer churn in the market – or the ability to compete those households away from other banks – not from demographic household growth.

Summary

There are many variables that go into understanding if a particular branch is meeting, exceeding, or underperforming expectations. If banks make the effort to understand true branch performance, given each branch's unique set of circumstances, they effectively take the first, critical step to establishing equitable sales goals.



UNITED STATES

One Global View
Troy, NY 12180
1.800.327.8627
pbbi.sales@pb.com

CANADA

26 Wellington Street East
Suite 500
Toronto, ON M5E 1S2
1.800.268.3282
pbbi.canada.sales@pb.com

EUROPE/UNITED KINGDOM

Minton Place, Victoria Street
Windsor, Berkshire SL4 1EG
+ 44.1753.848.200
pbbi.europe@pb.com

ASIA PACIFIC/ AUSTRALIA

Level 7, 1 Elizabeth Plaza
North Sydney NSW 2060
+61.2.9437.6255
pbbi.australia@pb.com
pbbi.singapore@pb.com
pbbi.china@pb.com

www.pbinsight.com