Avoiding Deposit Displacement: Increased Emphasis for All Banks
by Charles Wendel

Recently, I was speaking with a senior exec at a bank that has long focused on capturing low cost deposits from its customers. It is among the best at doing so. Therefore, I was surprised when he wanted to talk about how to grow his deposits. Why? In part because given their lending expertise and focus "We can lend as much as we want." But, he needs the deposits to generate the margins the bank expects. This bank is looking for deposits because of strong growth opportunities. However, many other banks are pursuing deposits defensively and reactively and lack a plan to address the systemic changes that are occurring.

We see too many banks that seem to be relying on customer inertia as a driver of their deposit strategy. Yes, in many cases deposits have been sticky, but there are societal and business changes occurring that will challenge most banks. The strategy that some banks pursue of paying a premium for a deposit rich bank may also make less sense going forward, as those deposits may not be as reliable as expected.

Here's one take on how circumstances around deposits may be changing. A month ago, Ron Shevlin, a speaker at the Source Media Retail Banking Conference discussed what he termed "deposit displacement." His point was that the consumer (and likely some small businesses as well) are already and will be increasingly moving their dollars out of banks and into other accounts. He mentioned Health Savings Accounts ($45B), Venmo and other P2P payment companies ($2B of unused funds in customer accounts), Starbucks loyalty cards ($1-2B), and robo-advisor options that can take funds out of banks, particularly as rates rise. The point of this and other analyses is that current levels of bank deposits are likely to erode, given the options available to depositors as well as their increased sophistication.

These options are, in effect siphoning off when used to be "bank" deposits to other more attractive or better-hyped areas. As more non-bank players explore the payments area, competition of this type will only increase. At the same time, baby boomers who have been such a dependable source of bank deposits, are disappearing as wealth transfer to a younger generation continues.

In addition it makes sense that as rates rise, more depositors will realize that they have been subsidizing the banks with their "free" deposits. Companies like Marcus and Capital One, among others, continue to broadcast the higher rates they are willing to pay. More of these messages will get through to the end customers and depositors will be receptive to these messages.

One question that banks need to ask themselves centers on whether they provide any value proposition around their checking or savings accounts. Most product people will say yes and may even have some customer surveys supporting that view, but bankers may be deluding themselves.

So, what to do? Just by reading business press, a banker could probably list 100 or more items for an action plan. Among them:

- Pump us incentives for RMs and branch managers for DDA growth
- Concentrate on maintaining current key depositors
- Focus on getting more of the wallet share of current customers
- Create a deposit-only sales team
- Focus on deposit-heavy segments
- Offer product packages that involve capturing deposits
- Use tiered pricing

And, so on.

All of these ideas may have some merit, but no bank can accomplish all of them. Banks operate with limited bandwidth and often lose focus on one area due to competing forces.

Where to start? In my career virtually every project has benefited from developing an initial "fact pack" that quickly and succinctly captures the current state of a business. To the extent possible a fact pack relies on quantifying performance, but facts are tricky things so the need exists to reach out to the key players involved in a particular area to gain their perspectives on the current state of the business. Oftentimes, internal perspectives will clash with one another. In that case bringing the key people into a room together to review current performance and the issues impacting that performance can create priorities for change.

This is not a case in which the consultant borrows a banker's watch and then tells him the time. Fact packs provide great value in setting a path: reviewing the numbers always results in some surprises and insights; in most cases, non-quantitative, organizational issues need to be highlighted and addressed for positive change to occur. Too often, the personnel and personal issues are ignored because they can be difficult to deal with.

Many banks are facing a critical deposit/cost of fund issue that will grow in significance. Step One: take the time to understand your present situation related to sources of deposits, recent trends, and organizational roadblocks and capabilities. Once accomplished, priorities for action will become much clearer.