Banks Need to Exploit the Power of Verticals
by Charles Wendel

This Thursday, Bankers Hub is presenting my webinar "The Power of Verticals". Banks that focus on segments/verticals/niches almost always outperform banks that cast too wide a net and fail to set clear customer focus priorities.

Why do focused banks outperform others? At least four factors result in better performance:

Lower origination costs. Specialization allows a bank to gain a reputation for serving a particular segment or business need. Outbound marketing becomes more targeted and effective as banks focus on a defined target set. In addition companies and individuals seek out a bank that has positioned itself to meet their needs or interests.

This type of segmentation applies both to the consumer and business sides of the bank. We have banks focus on consumers ranging from Aleutians to RV owners. Possible business segments are as diverse. Segmentation may focus on type of loan required (e.g., SBA, CRE, or structured finance), a company's stage of like cycle, and/or industry segments.

Higher risk quality and reduced losses. The "economy of focus" that segmentation creates should result in an improved risk portfolio. Two comments, though. Of course, poor credit discipline cans exist is bankers stretch due to overconfidence concerning their specialized knowledge. In addition, focusing on just one-two segments is precarious. Example: Companies that had highly concentrated taxi medallion loan portfolios suffered significantly; those lenders with more balanced portfolios saw overall earnings recover quickly.

Relationship based pricing. Many customers may not value their bank relationships as much as they did years ago, but value still exists. Segment-focused lenders demonstrate value in their knowledge or the specific credit ands non-credit needs of their customers and their ability to provide customized solutions.

Banks struggle with differentiating themselves from other provides. Smart segmentation creates that differentiation.

*Sustainable customer relations*hips. Replacing customers involves a costly and time-consuming process. The knowledge and, yes, wisdom, that a specialized banker can provide a client creates incredible stickiness fore the relationship.

How do you choose a segment?

No two banks possess the same capabilities or strengths; therefore, the areas they focus on should also likely differ. Common segmentation criteria include:

- ✓ Demographic
- ✓ Industry sector

- ✓ Company turnover
- ✓ Company lifecycle
- ✓ Loan type
- ✓ Linkages to existing clients
- ✓ Other firmagraphic characteristics, for example, company age, geographic location, etc.

Too often banks that segment select segments that many others are also focusing on, most notably, professions. Professionals can be a great segment, but succeeding with them requires time, investment, and expertise that not all banks can or should offer.

We suggest beginning by analyzing your current consumer and business portfolios. What types dominate your business today?

- If your consumers are aging, how are you focusing on meeting their needs while also reaching out to a younger constituency?
- If your business portfolio has a large number of restaurants (many do) are you offering them the best cash management services? If you do not want to lend to them, can you team up with a Fintech lender that focuses on that segment?

Beyond evaluating your current portfolio, what segments are being underserved by your and your competitors? What can you learn from the banks about areas to focus on? Look at companies like Live Oak with SBA, Aspiration with Millennials, Lendeavor in healthcare practices, and many others.

Here are some of the business segments others focus on:

- Professionals: lawyers, doctors, accountants
- Marijuana farms
- Funeral homes
- Women-owned businesses
- Ethnic-owned businesses
- Start-ups
- Spas and health clubs
- Restaurants
- Time share developers
- Franchise finance
- Churches
- Tow trucks
- Used agricultural equipment
- Strip clubs (!)

The list is never ending as more bank and nonbank players look for a competitive edge**.**

Consider this checklist in evaluating which segments to select as your own:

- Review your current customer base for segments/niches already served
- Determine which segment(s) the bank wants to focus on/should focus on
- Review bank capabilities/products

- Address gaps/role of third parties
- Evaluate staffing needs
- **Then, make go/no go/niche decisions**
- Consider select hires/lift outs
- Develop plan related to affinity groups/COIs
- Create marketing message/packaging
- Get the right internal people involved
- Revisit niches annually

In our view, segmentation is a necessity, not an option.