One Number Management
By Charles B. Wendel

Can you manage a bank by focusing on one number, one metric, that you focus on with laser like clarity? Of course not. The ultimate metric is profit and even there you need to look at profit over time. But there is one ratio that experience suggests indicates how well a bank is managed, how likely they are to be a long term player that provides value to shareholders and employment to staff. Beyond the bottom line, it is the first number I look at.

It is the operating expense ratio.

Banks with high OpEx put themselves at a competitive disadvantage to other players. Every dollar a bank with a high operating ratio earns is chewed up by internal costs, limiting the bank's net income and ability to invest in growth.

What's a high ratio? Banks with ratios above 50% should begin to pick apart their costs and see what drives expenses. Often, they can trace high costs to an overinflated senior management structure, one that is top heavy with bankers resting on past achievements rather than gearing up for the future. Universities have long suffered from offering life-long tenure to professors. Many banks continue to provide a similar level of life-long employment with the same unacceptable results, namely, employees "phoning it in" rather than continuing to push. Fintech's don't provide tenure and never will.

People and facilities generate the costs. The cost issue does not involve revenue producing people, those that sell, get clients to maintain and grow their relationship with the bank, and differentiate the bank from others. Mediocre sales staff, support personnel that, rather than support, act as a ballast to the bank, those are the people who need to depart. Again to mention universities, personnel budgets have exploded not to hire professors or to lower the teacher/student ratio but to hire more staff focusing on non-educational issues. When I was a banker, the world was simpler. The revenue generators were the acknowledged leaders.

Can an operating expense ratio be too low? Of course. But I would rather run a bank with a low ratio and increase it strategically than be running a bank with a bloated ratio that I needed to manage down, causing intense disruption to staff and customers. The banks with 60%+ ratios must invest in digital technology, but may lack the budget to do so. If they have allowed a tenure mentality to permeate the bank, they may also lack the talent required to transition to a digital world. Banks with lower ratios may have skimped on IT, but have the ability to increase spending in a targeted way manner, a great competitive position.

FIC has worked with clients of similar asset size that have distinctly different levels of operating expense ratios, almost at opposite extremes. In one instance the bank has allowed an internal governmental bureaucracy to grow within the bank to the point that the bureaucracy has overwhelmed the revenue producers. Management of the other bank never allowed that to happen, maintaining a world in which quality revenue and revenue producers rule.

Given recent events, one bank is cutting personnel while the other continues to expand, hiring revenue generators.

You don't need a consultant to tell you which bank has a brighter future and is more fun to work for.

FIC works with clients on these and related issues. Continued uncertainty requires organizational flexibility as financial institutions focus on their future performance and growth while managing current portfolios and changing customer expectations.