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Fire in a Crowded Theater

Banks who respond to regulation by raising checking fees risk a customer stampede—out the door.

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Instead of operating in a panic mode, the smart bank will see the new regulations as an opportunity to stand out from the rest.

We all know why yelling F-I-R-E in a crowded theater is illegal.

It's strange that banks facing regulatory change don't see the correlation between a standard reaction to new rules and a crowd stampeding to a few small exits to a competitor.

New banking regulations which, for instance, limit debit card or ATM overdraft fees have led many banks to conclude that the only alternatives are to eliminate free checking and add new fees for services that had been free or low-cost.

Views contrary to popular opinion are not necessarily wrong.

Let's examine the accepted latest assumptions about free checking.

- If the individual checking account isn't generating at least as much revenue as it costs to provide it, it's a loser.
- Banks can't continue to give away product for free.
- Banks have no choice but to raise other fees on these accounts or find new ways to make money from checking account customers.

This is hardly a new problem. As income from interest spreads between deposits and loans has proved insufficient over the years (and proved increasingly insufficient in the new financial environment), banks have been looking for new sources of income to fill the gap. The answer has always been to impose new fees.

In many consumer businesses, the marketing process includes identifying customers that can be served profitably when offered a mix of demanded products and services. The idea is that the customer is valuable and the relationship is profitable; not that every time the customer makes a transaction, the business will make a profit. Inevitably, the banking customer in the latter case will recognize the bank's motivation and look for alternatives.

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Surely, this is a contributing factor to the current situation in consumer banking where the average customer has relationships with three, four or more banks. After all, what bank customer in her right mind would endure the inconvenience of hopping from bank to bank if she didn't feel she was being nickeled and dimed for every product or service offered by her primary bank?

The cheap becomes expensive

One consequence is that customers who take their next banking needs to a competitor also place on the incumbent bank the need to go out and find new customers. It costs many times more to find a new customer than to keep and to sell to a current one, yet this every product/every transaction profitability orientation inevitably will lead to customer churn and poor penetration of bank products.

For other virtual commodity businesses like grocers, hotels or restaurants, examples of returns on loss leader pricing—products offered at steep discounts in order to attract new customers—are too numerous to count. Still, many in banking believe this is the path to ruin. I don't think so; partly because of some banks' inability to look at the total value of a customer.

Banks must weigh the costs and benefits of the "no profit" products against the costs and benefits of making the relationship attractive to those customers whose patronage deepens beyond checking to add credit cards, car loans, RV loans, mortgages, second mortgages, savings, CDs, investments, trust services, and commercial relationships. To execute this type of thinking, banks have to evolve beyond their typical siloed P&L organizations to customer-centric ones.

Banks do have choices. Here are three that come immediately to mind.

1. Segment the market. Find who needs what and the terms that are acceptable.
2. Discriminate. Sell item A only to those who truly want item A; sell item B to those demanding B, etc. This prevents the customer from "turning off" the bank that sends an endless stream of A, B, C, D, and E offers to everyone. For the customer who wants only items A, F, G, and H, most of the bank messages won't resonate. And, these useless messages tell the customer the bank doesn't know him.
3. Fit, don't force it. All customers evolve as they move through life. If the bank has solid relationships, retains customers, and responds to customer needs, increasing profit is virtually guaranteed.

Granted, this is a biased view coming from a life-long marketer. However, it is an efficient view. The segment-driven approach will ultimately target fewer, convert and retain more, and be simpler to grow and defend than continuously going after new customers, keeping a small fraction, and then sharing their business with four other banks.

Instead of operating in panic-mode, the smart bank will see the new regulations as a golden opportunity to stand head and shoulders above the rest.

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