haberfeld
accelerating growth

EBOOK

Unmaking a Myth:

Why You Don't Have to (and Shouldn't) Raise Fees to Increase Non-Interest and Fee Income

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Myth

There is a pervasive myth preventing growth for financial institutions today.

THE MYTH IS THIS:

Financial institutions (FIs) must raise fees in order to increase non-interest income.

Like many widely accepted myths, it originated from a moment of historic upheaval. We can trace it back to the 2008 financial crisis when FIs saw that circumstances had to change.

They assumed they **needed to increase fees to increase non-interest income** - and in some cases, survive.

However, two faulty assumptions made it very difficult.

THEY ERRONEOUSLY ASSUMED THEY HAD TO:

- Structure their products so they offered nothing at a loss, and
- Target only high-value potential customers

Meanwhile, big FIs are able to charge more fees because they have a higher perceived value to the consumer, based on technology, products, and larger branch networks.

Reality

The Bigs are Winning

Our research shows that between 2008 and 2019, the top 30 FIs increased their collective market share of domestic deposits from less than 50% to nearly 60%.

THE REALITY IS THIS:

While other FIs were raising fees and chasing short-term profits with every product and customer, truly successful FIs swiftly took majority ownership of the market by doing the following:

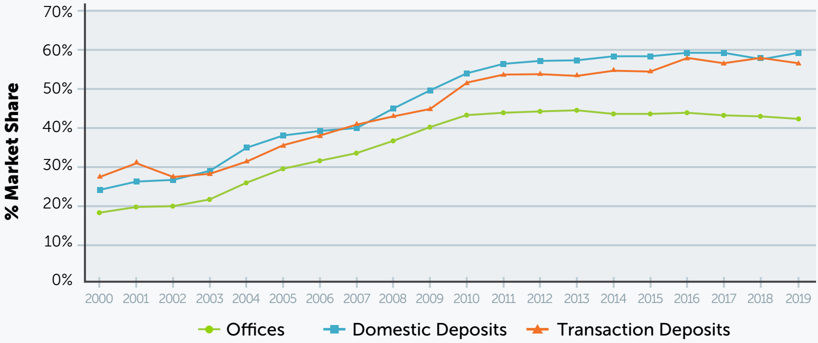
- Lowering or structuring fees around value vs. nuisance fees
- Aligning their policies and procedures to maximize fee income

THESE FIS UNDERSTOOD A KEY FACT:

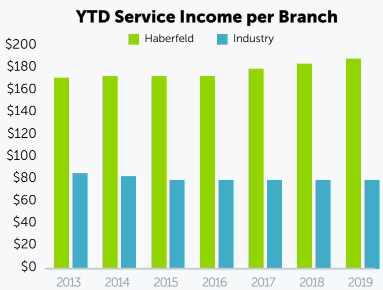
Customers want an FI that will value their business. They don't want to be seen as just another revenue source.

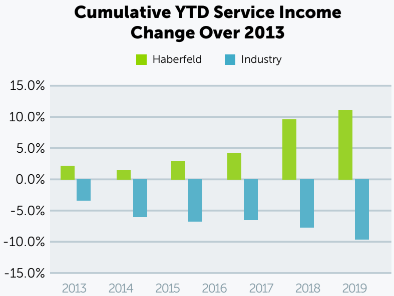
Even so, many FIs refuse to believe a value fee vs. nuisance fee model can work for them

Top 30 Market Share



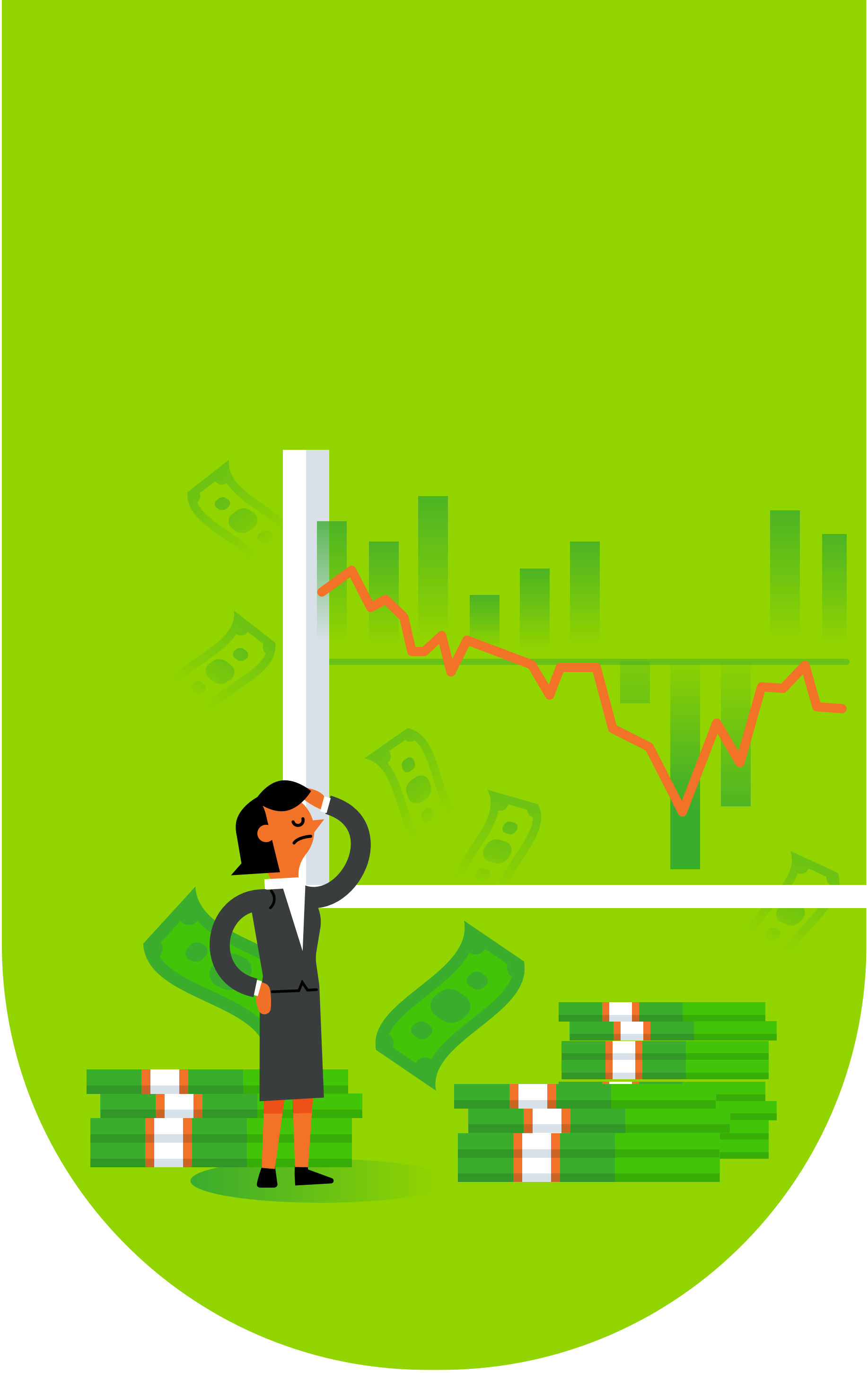
Service Charge Income per Branch Trends





For the average $1B FI, the difference from a Haberfeld client to a non-Haberfeld client is more that $1,000,000!

> Institutions that focus on valuing customers have significantly more of them; and as a result, generate more service charge income.



How the Great Recession Changed Things

In one analysis, authors Joseph G. Haubrich and Tristan Young concluded that FIs which experienced smaller net interest margins and decreased interest income—due to the financial crisis—may have compensated by increasing their reliance on non-interest income.

As we mentioned above, this made sense at the time, especially since non-interest income is less susceptible to market fluctuation. However, while increased nuisance fees provided short-term relief in 2009, it was ultimately not viable for long-term growth.

IN A REPORT PUBLISHED BY THE FEDERAL RESERVE BANK OF MINNEAPOLIS, STEVEN ENFIELD NOTED:

> *The noncyclical nature of non-interest income enhances its appeal for community FIs. This appeal is tempered by customer preference for lowered transaction costs... Non-interest income continues to contribute to the revenues at community FIs, albeit at a lower level than in the past.*[2]

Community FIs know fee income has value, yet they understand they must accommodate their customers' expectations.

Making Change

Since most customers expect no-fee banking, you might assume a community financial institution's wisest strategy is to only pursue higher-value accounts to increase net interest margin.

If that's your assumption, it's time to reassess. **Here's why:**

Searching for the perfect customer within your geographical market is an exercise in futility - unless all of your branches are located near high-value customers.

INSTEAD, EMBRACE THIS MYTH-BUSTING IDEA:

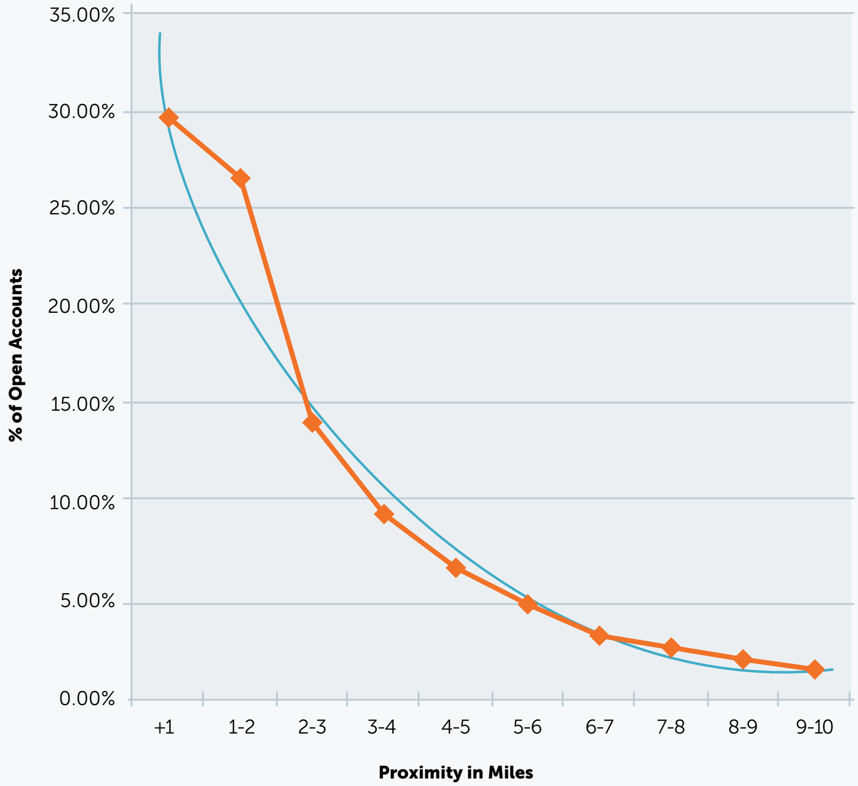
- To grow fee income, your community financial institution should increase its core checking customer base, not just fees

Yes, you will add a small number of unprofitable customers, but not at a faster rate; they'll grow proportionately with your overall customer base.

Further, once your branches are running at increased capacity, your overall non-interest income will more than make up for any losses sustained by adding a few unprofitable customers.

HOW DO YOU MAKE GROWTH HAPPEN?

Convenience is still #1



Utilizing a Factory Mindset

Let's borrow a page from our friends in the manufacturing world.

As a community financial institution, you most likely operate a number of underutilized "factories" just waiting for increased activity and output—and by "factories," we are referring to local branches.

GOOD NEWS: Rather than losing sleep trying to determine which prospects will generate the highest revenue, focus on using your branch to its maximum potential. You will find—and the data shows—each prospect who comes through your doors or online channels requires a marginal cost to be served and will bring a meaningful return on investment.

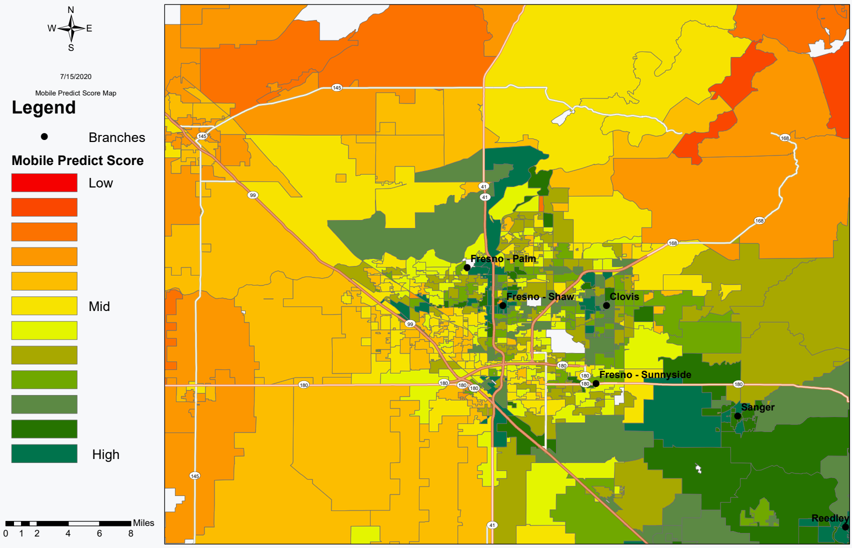
FIs should focus on maximizing the output of these "factories" by looking at their branches as Sales Centers. In-branch transactions per customer continue to decline due to technology investments, but the branch is still very important for new checking customer acquisition.

BETTER NEWS YET: The marginal cost to serve new customers is very nominal.

> *Our data shows the average marginal servicing cost per checking account is approximately $30–$50 per year.*

At such a low cost per new customer, why wouldn't you want to grow your overall customer base? In due time, this growth is guaranteed to generate higher-margin business and further retail accounts at your FI.

BEST NEWS: A typical retail customer will bring $300-$500 in marginal income each year.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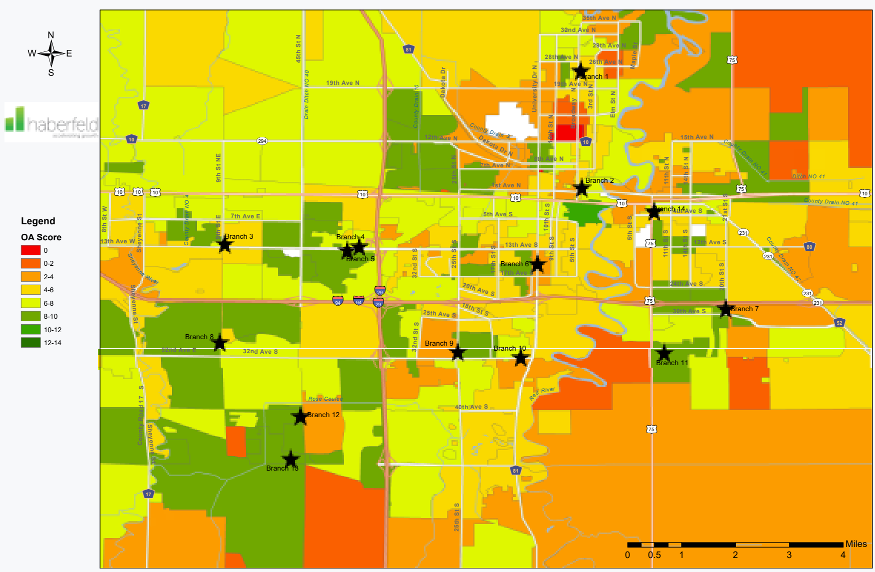
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Attracting New Relationships

Once you've successfully shifted your mindset, the next step is to position your FI to appeal to new customers. **SO, HOW DO YOU DO THAT?**

1. Make your product stand out. What can your FI offer that other institutions in your area can't? Whether that's your products, technology, service, or an interesting incentive, make sure to promote your compelling offer.
2. Use marketing analytics to identify which prospects are most likely to choose your FI, and tailor your messaging to speak directly to them.
3. Focus your efforts on people who already want to switch and will soon choose a new FI versus trying to convince people they should switch.

With patience, intention, effective messaging, and targeted campaigns, you're sure to grow your customer base in time.

For more on this topic, please check out another one of our eBooks:**"5 Essential Strategies for Core Deposit Growth."**

Measuring Success

With a wider customer base in your area, you'll notice many benefits.

MORE RETAIL AND BUSINESS RELATIONSHIPS

When your FI grows its community presence, you'll earn more accounts to provide more products and services as well. And, as you earn more business, you'll earn more trust, and the trust of your neighbors and customers will further grow your business.

FUNDING LOANS

While not every new checking account will be individually profitable, as a whole they help provide extremely low-cost deposits to fund loans. For banks, the average balance for a personal checking account is $4,361 and a business checking account is $21,038. Collectively, these balances provide a powerful source to lower cost of funding.

FEE & NON-INTEREST INCOME

Here's that coveted fee income! The average fee and non-interest income for retail accounts for Haberfeld clients was $144.30 for banks and $166.33 for credit unions in 2019. That's extra fee income without raising fees.

Many FIs that follow this strategy also experience a separate success metric that contributes significantly to the bottom line - an enthusiastic workforce!

Bear in Mind ...

As you use this mindset and strategy to increase non-interest income (all without raising fees!), you will need to keep these facts in mind:

YOU WILL acquire a small number of unprofitable customers.

> **HOWEVER:** You will also significantly increase your total volume of profitable customers. You will also likely increase your gross overdraft and interchange income with this increased volume.

YOU WILL lose some revenue after eliminating certain nuisance fees, but these fees are a small revenue driver of overall profitability per customer.

> **HOWEVER:** You will make up for this dip in average profitability by increasing the overall volume of customers—and increasing your total profits.

Letting go of these community-banking myths will allow you to forge a clear path to raising your income—and when you see the results, you'll be very glad you did.

The Big Picture

In this eBook, we've outlined the importance of your day-to-day factory mindset while zeroing in on the value of expanding your customer base.

NOW, LET'S TAKE A STEP BACK.

Right now, you know that each of your customers demands a low average cost and provides you with substantially higher average annual revenue.

But when you grow customers, you're not just collecting a one-time fee; you're creating an annuity by developing long-term relationships with people who will return to you for new deposit and loan products. And with greater community visibility, you'll earn even more highly valuable retail and business accounts.

To further prove our point, **HERE ARE THE RESULTS YOU SHOULD EXPECT:**

- New customers stay with their FI **ON AVERAGE ALMOST 10 YEARS.**
- The net-present value of a **NEW RETAIL BANKING CUSTOMER IS APPROXIMATELY $3,300; FOR A NEW FI MEMBER, IT'S APPROXIMATELY $2,600.**
- The net-present value of a **NEW BUSINESS CUSTOMER IS ALMOST $12,000; FOR A NEW BUSINESS MEMBER, IT'S MORE THAN $7,500.**

This is why we work so hard to expose the myth. We want to give you long-term value.

Haberfeld Math 101

$100 Amount our average client invests to acquire the next core customer

$250 Amount that customer generates in checking revenue per year

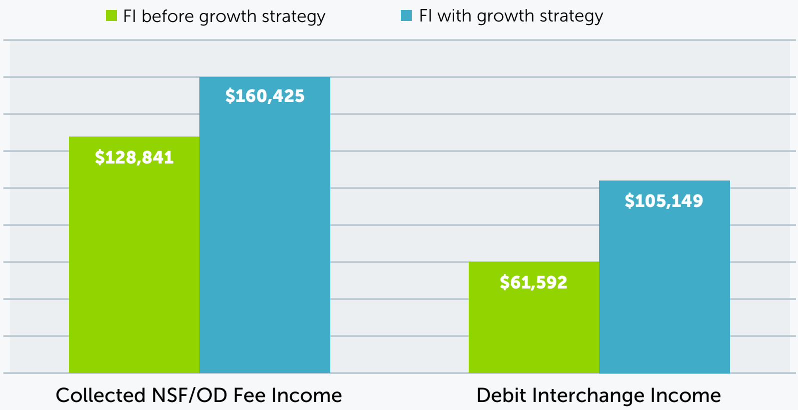
9+ years Average number of years a new customer stays with our clients

$3,300 Net Present Value of your next Retail Customer.

$12,000 Net Present Value of your next Business Customer.

Non-Interest Income

Monthly Income Comparison



Difference of 900k annually!

> The most important thing you can do to grow your non-interest income is expand your customer base without frustrating your loyal customers with new fees.

Shaping a New Reality Together

Most community FIs want and need to increase non-interest income, and we want to help them do it in a way that generates greater results without the added fees.

If you're in this for the long haul, put the old myth aside and set your sights on a new approach.

At Haberfeld, we have a 10-step process that helps FIs generate success, drive new-customer traffic, and establish healthy, sustainable momentum.

REACH OUT TO US TODAY and get ready to accelerate your growth!

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