

BANKS UNLOCK CUSTOMER PROFITABILITY

Measuring and managing the profitability of individual customers can positively impact a bank's performance. When banks make information about their customers available to the front office in an understandable manner, they enhance these opportunities dramatically.

According to Kyle Duckers, senior director, Financial Services Industries for Oracle, a vast number of customer relationships are unprofitable for banks. In fact, only a tiny percentage of accounts are profitable, although most are only marginally unprofitable.

"For most banks, it's traditionally been an 80-20 rule, with 20 percent of customers making up 80 percent of the profits, or even closer to 95-5, with 5 percent making 95 percent of a bank's profits," Duckers says.

Profitable accounts provide a challenge for banks because customers with money-making accounts also have the highest attrition rates. Banks, therefore, must provide top service to these account-holders. The first step is to identify them. Then it's essential the customers' status is communicated to customer-facing bankers.

Still, marginally unprofitable accounts provide the greatest opportunities. Accounts that might be losing a little money for the bank can be turned into profitable accounts relatively easily. Even modest gains in profit, multiplied by vast numbers of customers, can result in big, bottom line results.

Identify Profitable Customers

Identifying profitable and marginally unprofitable customers, finding out and having a good idea what services they may be interested in is the key to unlocking the profitability of their accounts. In order to transform these accounts banks need to drive them to a profitable configuration of products and services.

But identifying profitable customers requires more than a quick glimpse at an on-screen account snapshot. A bank must use funds transfer pricing methodologies, and look at how frequently each customer uses its shared services and delivery channels like ATM, Web, call center and branch teller. A bank must also know how much each transaction costs.

Unlike the retail industry, banks can't identify their customers' profitability at the point of sale. "When you buy an item at a store, the return that customer provides is known immediately. How-

ever, when a financial services firm signs a new customer, it doesn't immediately know, Duckers explains. "The customers' profitability depends in great part on the delivery channels they use and how often they use them. It is also important to know the value of the customer over the lifetime of the relationship so decisions aren't made based on point-in-time aberrations."

Profitability information is usually analyzed strategically by key banking executives who use the information for decisions including where to deploy its capital to what businesses it enters or exits. While it's strategically necessary for top executives to know the profitability of its customers, it's critical to make this information accessible to the front office, branch employees and call center representatives.

Customer-facing employees can tailor their service levels according to the value and profitability a customer provides. They can provide exemplary service for the most profitable customers. They can also maximize cross-sell and up-sell opportunities by offering products uniquely suited to each customer's needs. Front office staff can also use profitability information to determine how to get marginally unprofitable customers onto a profitable footing.

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also offer a product he or she may need next. If a customer has children approaching college age, a representative might offer a student loan or home equity loan, for example.

"These are the kind of tactical profit opportunities that banks need in order to increase the number of profitable customers," Duckers points out. "If you know how much a customer is costing the bank, then you know how to price accordingly. If a valuable customer wants a fee waived, for instance, front office personnel can have the information at hand to know if it makes sense to do so."

Make Information Available, Understandable

Top executives, managers and front-line bankers should all have access to customer profitability information, although they use it in different ways and for different purposes. They have to see the same profitability information, although it should be offered in a format tailored for their use. The information has to reconcile and tie back to the general ledger in order to be credible. Most important, it must be understandable to the recipient.

Top-level bank executives will use customer profitability information to make strategic decisions. Key banking executives use profitability information to for business analytics and to evaluate risk.

“Senior executives might look at profitability information, then look at a product and determine if it’s one they want to continue to offer,” Duckers says. “But front-line bankers will use the information in a more granular way, on a customer-by-customer level. The appropriate amount of capital to apportion to each customer to reflect their relative risk is also crucial so profitability is measured on a risk-adjusted basis. This granular allocation of equity is consistent with Basel II requirements, which are becoming an industry accepted best practice, regardless of the bank’s need to comply with the accord.”

Front office personnel may not be familiar with profitability metrics or risk-adjusted return on capital, but they can relate more easily-understood terms. Bank tellers and call center representatives can benefit from information presented to them in an understandable format. Delivery mechanisms like dashboards and scorecards are gaining acceptance as best practices for delivering this information.

Easily-understood profitability information can be a boon to

front-line bankers and help them take advantage of tactical profit opportunities. If tellers or branch employees know a customer is profitable and sees the products the customer already has, they know the customer may be a candidate for another product.

Profitability information must be presented in a no-nonsense fashion to front-line bankers for maximum results. One large East Coast financial institution uses profitability information in its call center, where employees assign customers into Gold, Silver or Bronze categories.



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Oracle has the tools to bring profitability information to the point of customer interaction. Oracle Financial Services Applications (OFSA), Oracle’s integrated suite of financial, accounting and risk management applications includes Oracle Profitability Manager and Oracle Funds Transfer Pricing.

Oracle Profitability Manager is a comprehensive, flexible solution for profitability calculations, activity-based costing and analysis. The tool delivers multi-dimensional analysis capabilities,

including profitability by customer, product, sales channel and more.

Oracle Funds Transfer Pricing tool enables banks to properly calculate profitability by enabling them to assign a value to funds provided by depositors and a cost to funds used by asset-generating units. With this tool, lending institutions can more effectively set prices and structure products.

In addition Oracle Business Intelligence Enterprise Edition (formerly

Siebel Business Analytics), delivers industry-leading analytics to the front line in a credible, timely, understandable fashion. The combination of OFSA and Oracle Business Intelligence now provides an unprecedented solution for delivering powerful information to where it is needed: the point of customer contact.

A major player in the financial services arena, Oracle currently has more than 250 customers using its Customer Profitability Solution.