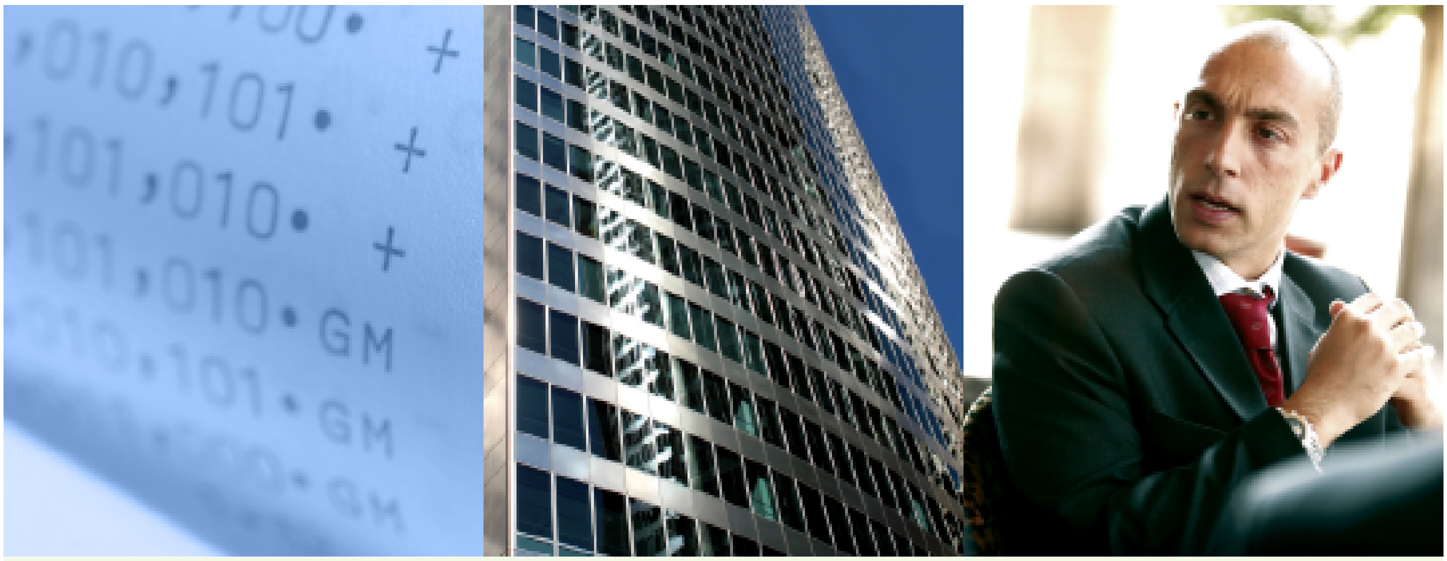
FPS THE EXPERTS in Loyalty-Building Financial Communications



The Cost of Customer Churn

What's at stake for banks in the competition for customers?

A Financial Publishing Services White Paper

Overview

Today's savvy corporate clients demand greater value and tangible solutions from a reduced number of banking partners. While this desire by corporates nets banks fewer customers overall, the potential revenue gains banks can realize from these finite relationships have never been greater.

At the same time, however, the financial implications of customer churn related to a shrinking and shifting client pool means bank marketers have much to lose if they fail to modify their methods for retaining existing relationships. To win the trust and business of CFOs, bank marketers must migrate away from traditional, product-oriented communications and toward more informative, solutions-oriented messaging such as newsletters, Webinars, white papers and case studies. After all, clients aren't interested in buying products; they want proven business solutions.

Banks that shift away from a product-centric culture toward a customer-centric model will be better positioned to maintain client loyalty and grow their bottom lines organically.

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Competing for customers

Maintaining banking relationships is challenging amid escalating corporate merger activity in many industries. This is particularly evident within retail, manufacturing, communications, technology and healthcare businesses.

As entities merge, their demands upon banks increase as they seek to reduce operating costs and streamline their business processes.

In addition, many CFOs find themselves second-in-command to the CEO, and responsible for accurate forecasting and strategic planning for the entire business.

CFOs use their access to new technologies and more sophisticated financial accounting and analysis software to focus on the long-term bottom line more easily.

With broadened responsibilities and limited time to address marketplace complexities, CFOs are turning to their financial institutions to help them maintain a competitive edge.

In a 2005 interview with MarketingSherpa, Caroline Smith, Director of Marketing for *CFO* magazine, says CFOs want information on issues that impact their own company's and their industry's long-term financial success. Says Smith, "those who can deliver relevant information in a concise and direct format will be the most likely to get the attention of today's CFO."

The commoditization of banking is another trend impacting client attrition and acquisition rates. Some industry reports estimate that banks are losing customers at an average rate of 12.5% per year, while average acquisition rates are at 13.5%. Furthermore, the cost of acquiring new customers is estimated at five times the rate of retaining existing ones.

Banks must find ways to stop the bleeding because loyal customers spend more on higher margin products and are likely to refer additional customers.

The only answer is for banks to nurture deeper, more consultative relationships.

Monetizing customer churn

Banks must find ways to consistently touch their clients to keep them connected to the brand. In the book, "The Loyalty Effect: The Hidden Force Behind Growth, Profits, and Lasting Value," author Frederick Reichheld says customer churn rates decrease drastically when customers have this connection. As little as a 5% reduction in customer churn can boost net profits by as much as 20%, Reichheld notes.

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— Caroline Smith, Marketing Director, *CFO* magazine

In banking, a similar reduction in customer turnover can increase net profits as much as 80%.

How do these numbers impact actual bank revenues? Perform the following calculation to determine your own institution's potential revenue gain by reducing customer churn for a typical commercial client:

Average Annual Revenue Stream Generated x Estimated Life Span of the Relationship = Life Time Value (LTV) of a Client

By calculating a client's Life Time Value (LTV), you can see how even the smallest decrease in customer churn can improve your bottom line significantly.

If you are not sure of your average annual revenue stream per client, use data from the 2006 Treasury Strategies Benchmarking Database. For example, for middle-market clients (annual revenues of up to $1 billion), the average annual bank profit on an active account is $5,723, Treasury Strategies reports. Using the calculation provided and given that the average life span of a commercial relationship is eight years, the LTV of your average middle-market relationship is $45,784:

$5,723 x 8 years = $45,784

For large corporations (annual revenues exceeding $1 billion), the average annual bank profit on an active account is $63,677. Using the same eight-year relationship life span, the LTV of your average large corporate relationship is $509,416:

$63,677 x 8 years = $509,416

Banks can add more than $1 million to the profitability of their commercial banking business line by simply extending 16 of these large corporate relationships by one year.

Given these figures, it's logical for banks to focus on retaining current clients and growing their share of wallet from those customers. Dollars generated by extending client relationships is easy money when you consider the probability of acquiring sales from current clients versus prospects or former customers.

Jill Griffin and Michael Lowenstein state in their book, "Customer Winback: How to Recapture Lost Customers—And Keep Them Loyal," that the average company has between a 60% and 70% probability of success selling more services to a current customer.

These figures drop to a 20% to 40% probability, and then to a 5% to 20% probability, when selling to former customers or prospects, respectively.

Marketing's role in client retention and loyalty building

Despite these figures and the obvious benefits banks generate from serving current customers attentively, some banks fail to earn and keep clients' trust—and therefore risk losing their business.

One industry survey reveals that while bank customers would do all their banking with one institution they trust, only 28% feel their bank is trustworthy and consistently acts in their best interests.

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These figures are alarming and require action. Bank marketers must change this perception by differentiating themselves as a "trusted advisor" to business customers, and offer clients needed tools and information to help them succeed.

Becoming more relationship-oriented lets banks build trust, reinforce their brand as a business partner and gain more business.

Clearly, the more embedded you become in your clients' business processes, the more likely those clients are to remain loyal to the partnership.

The way to do this is by providing consultative marketing messages that guide business customers through the pain of changing (buying) and walk them through the daunting consideration path.

Such messages better prepare clients and prospects for a sales engagement, which reduces banks' sales costs and increases conversion rates.

Following up on leads with consistent, relevant dialogue—e.g., through newsletters, case studies, news articles, competitive information and Webinars—results in higher close rates regardless of the timing to buy, according to Bulldog Solutions' "The Evolution of B2B Marketing," a 2006 report.

As discussed in a recent Bulldog Solutions Webinar about the report, between 20% and 80% of leads nurtured by the methods listed above result in a sale. In contrast, cold leads buy less than 3% of the time.

Who's winning the battle?

Several leading banks are transitioning from a product-centric to a customer-centric culture. While the task is difficult and ongoing, early results are promising.

KeyBank

Kevin Riley, a KeyBank Executive Vice President, recently shared information about how the institution reshaped its marketing strategy during a 2006 KeyBank Webinar titled, "Customer Centric Banking." Between 1999 and 2002, KeyBank was losing market share, revenues stagnated and growth expectations were low, Riley explained.

The average company has between a 60% and 70% probability of success selling more services to a current customer, a 20% to 40% probability of selling to a former customer, and a 5% to 20% probability of making a sale to a prospect.

— from the book

"Customer Winback"

So senior management enlisted support from the bank's CEO to restructure the organization's focus from a product-centric to customer-centric enterprise. Customer groups were segmented by needs and marketing messages focused on addressing those needs.

Building on its image as a trusted advisor to corporate clients, KeyBank began issuing a wide range of consultative communications including two monthly e-newsletters, three industry-specific quarterly product updates, special reports and client case studies.

These client communications have increased corporate sales. According to a Greenwich Research study Riley cited during the Webinar, KeyBank has reduced customer churn from 13% to 11%, while increasing the number of services per client.

The bank simultaneously increased its number of new relationships by 5% and significantly improved its service excellence ranking. Riley reported a 12% increase in customer satisfaction.

Wells Fargo

Wells Fargo is another example of where Sales and Marketing reorganized away from a traditional product-centric focus to a customer-centric orientation with success.

In 2003, Wells Fargo launched what the bank's President and Chief Operating Officer John Stumpf calls "the customer experience." A 2006 case study on Wells Fargo published by CustomerThink Corp. reports how the bank interlinked its business units to create a more seamless customer experience. The bank estimates that for every 1% reduction in customer churn it will add $20 million to net profits. During 2004, the first full year of the new initiative, Wells Fargo improved its client retention by 6%.

"I can't think of anything that will have a bigger payoff for our team members, for our shareholders, for our communities, and for our customers," Stumpf told CustomerThink.

Since shifting to its new customer-centric focus, Wells Fargo has enjoyed double-digit growth in both revenues and profits. Additionally, employees were motivated to buy in to the new program because their compensation was tied to how effectively they retained current customers, says Jay Freeman, a Wells Fargo Vice President of Sales, in the CustomerThink report.

This customer-centric focus continues. Note the style of a recent Wells Fargo *Frontiers* newsletter:


FRONTIERS

...At Wells Fargo, our goal is to grow with our customers... This issue showcases the successes of three rapidly growing customers—from three very different industries—and highlights the strategies they've used to keep their momentum going year after year. ...Also in this issue are articles about optimizing use of your cash in a rising interest rate environment and a new electronic deposit service that can help you streamline payment processing and accelerate your cash flow. ...We are proud to be able to contribute to your success today—and in the future.

Clearly, Wells Fargo's Commercial Marketing Group is dedicated to conveying informational value to its business clients. For the past nine years, the bank has published a quarterly paper newsletter that delivers news, case studies and updated product information to its audience of commercial banking and treasury services clients.

Bank of Montreal

In its 2004 annual report, the Bank of Montreal (BMO) referred to itself as the "only financial services provider our customers will ever need." The bank's recent success in realigning to a customer-centric focus is consistent with this assertion.

While bank customers would prefer to do all their banking with one institution they trust, one survey found that only 28% feel their bank is trustworthy and consistently acts in their best interests.

Matt Fabian, BMO's Senior Manager of Customer Acquisition and Development, shared some of the bank's strategies and results in the January 2005 edition of *1 to 1* magazine. Marketing, which led the effort, first established customer research teams. "We went in with a war-room mentality," Fabian says.

The bank identified a variety of customer profiles, segmented clients by those profiles and began delivering targeted, relevant messages to each group.

BMO's Commercial Marketing efforts include an online tool called a "Solutions Match" that enables businesses to self-prescribe solutions based on a number of profile parameters. The bank also offers an online "Business Coach Series," consisting of e-books, worksheets and reports designed to help businesses optimize their financial resources.

Since beginning its customer-centric initiative, BMO has improved its market share by between 10% and 15%, and decreased customer attrition by 30%. The new focus also enabled BMO to bring new products to market four times faster than before, the article says.

Deliver solutions, not just products

These real-life examples prove that increased client retention and customer loyalty will be the keys to survival in business banking going forward. Corporate customers will continue to reduce the number of banks with which they do business, while at the same time demanding more from their remaining banks.

Accordingly, the survivors will be those banks that move from a product-centric culture to one in which the customers' needs come first.

For marketing, this means consistently touching clients with the business tools and information they need to succeed. Only then can banks strengthen and lengthen client relationships, gain a greater share of wallet, and ultimately position themselves as the banking leaders of tomorrow.