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Need Help In Identifying Branch Closure Candidates?

Everyone recognizes the importance of selecting the correct site for branch development. However, a far smaller number recognize the importance of closing the right facility or facilities to decrease operating costs within a specified market area.

Reducing Costs – Closing Branches

Cutting costs by closing branches sounds simple, but it can be a risky activity.

In many instances, what appears to be an obvious cost reduction opportunity is just the opposite. When looking more closely we find that many seemingly “easy” selections will have serious long term negative impact on system-wide branch performance. Closing a specific unit can affect the performance of other market area facilities.

Critical Mass Performance in Mature Markets

The long term negative impact from the closure of an individual branch facility is due to the breakdown of critical mass distribution, when the subject branch is a member of that group.

The benefits of critical mass, planned or unplanned, are achieved within an entire market or market segment. Critical mass is derived through the clustering of branch facilities and other service points, such as ATM's. These clusters are considered by both present customers and business prospects to be so located as to provide optimum service points both from a perceived “time and distance” perspective.

A branch can become part of a critical mass structure through:

- Perceived convenience to customers on a time and distance basis;
- Being part of a network of branches, ATMs and other service points;
- Geographical features, both man-made and natural elements, which affect travel and shopping patterns within a market area;
- Service offerings at branches within market area;
- Composition of competition; changes in competition; and/or
- Branch focus: business, consumer, high-balance/high-value

If it is suspected that a branch is within a critical mass structure, then the group can be analyzed to determine how they are functioning compared to potential. If the branches function up to 15- 20% above projections, then the critical mass halo effect can be confirmed.

A Facility Closing Can Fracture the Critical Mass Structure

The closing of one or more units contributing to Critical Mass, could adversely impact the achievements of all of the facilities that are part of that network. The downside to the remaining group could average as much as 12-15%, for all of the branches within the group.

System Operating/Overhead Costs

Another factor is the overall system operating/overhead costs. If a branch is marginally profitable, it is making a positive contribution toward operating/overhead costs. When that branch is closed, its contribution disappears. This places the burden of system operating/overhead expenses on fewer branches, thus increasing the per branch required contribution. A higher contribution rate makes more branches look marginally profitable, causing a vicious cycle with the branch network.

Does a Closure Candidate Have Upside Potential?

The first thing we do at GRFI is determine whether there is untapped potential within existing unit(s), giving special attention to the unit(s) that do not seem to be pulling their own weight. Can the performance of the marginal unit or units be improved within reasonable cost parameters in a way that will achieve profitability?

As part of determining upside potential, it is important to consider the marginal branch in relation to other branches within its market. Is it functioning within a critical mass structure?

Average Untapped Upside Potential

Experience has confirmed that on average any system with 10 or more facilities often has an upside profit potential of at least 20%. During a period of tight margins these opportunities are instrumental in achieving higher levels of profit with a small capital investment.

In larger systems of more than 20 units, we often find trade areas with some individual units having untapped potential in the 30% range. Larger systems see combined profit increases in the 25-30% range.

Can a Closure Candidate be Relocated or Consolidated?

Another alternative to outright closure, is to relocate or consolidate underperforming branches. Many times underperforming branches are simply in poor locations. In some instances we find that two branches can perform better when consolidated. The consolidation or relocation of existing facilities is far less traumatic than branch closures. In addition, relocation or consolidation do not project as negative an effect on the balance of the branch system as does a closure.

However, should a marginal facility be located within an area scheduled for additional or continuous development, a note of caution is also advised. The lone marginal unit will almost always see significant performance improvement as additional facilities are brought into its sphere of influence. This is especially true if additional strides are taken toward the achievement of critical mass within these newer trade areas.

Can the Closure be Repositioned?

If the closure can be “spun” in the right way, the negative impact may be minimized.

GRFI Ltd.'s Regression Modeling Identifies Untapped Potential

GRFI's Regression Modeling is an accurate way to project the potential of branches, which may be candidates for closure. GRFI can uncover specific untapped product-service potential that could be realized through new or renewed sales efforts and/or marketing techniques. We can also confirm management's decisions on which branches to close.

The models are a site specific assessment tool, the ultimate goal of which is to determine the value of any piece of real estate by projecting its deposits and related business revenue.

Each model will have sub models based upon the environmental classification of the market or the property.

For the standard GRFI Regression Model we assess and input 42 different characteristics in four major categories:

- **Trade Area Factors** include demographic data for the trade area.
- **Competition Factors** include the number, type and proximity of competition.
- **Site Factors** include the physical attributes of the piece of real estate such as visibility and traffic count.
- **Special Advantage Factors** include things such as proximity to retail draw and landmark reference.

Trade Area Factors and Competition Factors combine to create a Market Score. The relative strength of the market within our regression model accounts for an estimated 60-75% of the existing facility-market potential.

The true benefit to our modeling is the Site and Special Advantage Factors included in our analysis. As stated above, all sites within a market are not created equal. Our modeling includes a physical evaluation of each site. It is more than just selecting a successful market, it is selecting a piece of real estate that can deliver *the potential* of the market.

The reverse is also true. Because of the weighting of our four factor categories, a good site cannot outrank a relatively poor or marginal market.

The GRFI Ltd. Point Score is then related to a dollar-per-square-foot figure based upon the conversion tables established for different size facilities and their corresponding environments.

GRFI Modeling data allows the user to determine aggregate market potential by product, on both a dollar and index basis, so that the financial institution can set realistic share goals and objectives for each site evaluated.

Financial Impact of New Branch Operations

With business potential data in hand, GRFI runs a Breakeven, Payback and Capital Recoup Analysis to simulate future branch operations and forecast revenues for the facility. Comparing refurbishing and operating expenses against newly projected revenues, revised operating strategies can be implemented within realistic and manageable timelines and resources.

Prioritize Development Opportunities

With the projected revenues from one or more potential sites, optimum development and closure strategies may be implemented to maximize and prioritize profit potential while decreasing unproductive operating expenses.

For more information relating to “Branch Closure Evaluations,” contact George Frerichs at GRFI – 312.856.1444. Email – gfrerichs@grfilt.com