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EFTS is causing many banking concepts and practices to be rethought—including branching.

**Branch Planning in the Age of EFTS**

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Branches are becoming less of a financial commitment as more banks invest in electronic funds transfer systems. The goals of a bank in establishing branch offices in the past were to ensure a captive customer base. However, as EFTS becomes more widespread, the need for a more strategic approach is evident. The objective of branch planning in the age of EFTS is to maximize profitability and ensure future growth.

**Objectives of Branches**

According to the Federal Reserve Board's branch application form, one reason for branching is to relieve "head-office congestion." Another reason, according to the Comptroller of the Currency's branch application form, is related to the more efficient servicing of a bank's existing business. However, almost all banks will probably agree, the ultimate motivating for branching, which certainly encompasses these and other reasons, should be to maximize profitability and return on investment.

In technical terms, this objective involves the application of risk-adjusted capital-budgeting techniques. It is essential that the branching decision for a bank be put into proper perspective. This leads to one key point: Branching is but one means to profitable growth.

According to the "marketing" concept, profitable operations are the result of efforts to satisfy consumer needs. This involves the development of separate but integrated strategies for an organization's product, the promotion of its pricing, and finally, its distribution. In banking, the distribution of the services provided by a branch is a question of branch and service will not be strategized. Thus, the development of an optimal branch system involves more than the four marketing-mix variables.

Another way to see this point is through considering a bank's area of effective market coverage or "sphere of influence." In the case of a new office, this area is not yet defined, but rather, one in which existing and proposed facilities will play the most important role relative to both existing and non-existent electronic service units.

Of course, much will depend on the reasons for a branch in the first place, and what a bank can do to realize its goals.

**The Electronic Service Unit Mix**

(1) Off-premise electronic service units (CBCT) (2) CDM (Unattended) (3) ATM (Unattended) (4) NDF (Affiliated) - One service unit per store

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The Traditional Service Unit Mix:

1. Full-service facility (branch)
2. Limited facility
3. Mobile facility
4. Drive-in facility
5. Pedestrian facility

Considering the entire service unit mix in such a possible situation is most important.

Risks of Units and Point

Looking at electronic service units and points, it is possible to identify certain major risks they can potentially play in a branch system. The first risk that such equipment can play is purely of a support type, in terms of the enhancement of performance of the main office or a particular facility, such as a "problem branch."

Branching is not one avenue to profitable growth.

Electronic service units in this instance may be established as in-lobby, through-wall, drive-in, or parking-lot installations on the premises of the facility. The vast majority (over 90 percent) of existing CDMs and ATMs are on the premises of existing facilities. The purpose of these units is the ultimate enhancement of service, not only of a particular office but more importantly, the improvement of the bank's bottom line as per the system's view.

A second role of such equipment is both supportive and generative in nature, and is primarily related to increasing the market share in an area already served by the bank. CDMs and ATMs, in this case, are located off premises, but within the primary service area of an existing facility.

In many respects, however, the greatest profit potential of electronic service units lies in the development of new business in areas not being served by the bank. This is the third role of such equipment a purely generative role. Here, off-premise CDMs and ATMs are established outside of the primary service area of an existing facility.

Of course, banks in branching systems with a large branching system established over several years did not have the opportunity of planning their existing branch network with the roles and potential of electronic service units in mind. However, upon considering these factors, it appears that numerous decisions regarding the location and characteristics of a bank's existing and proposed traditional facilities will certainly be affected by the advent of EFTS.

This suggests that these banks that consider the impact of EFTS on their existing and planned traditional branches and service units will be in the best position to maximize profitability and return on investment.

Alternative Strategies

Before discussing alternative branching strategies in the age of EFTS, let us consider a key tactical question which must be answered regarding electronic service units. Should a bank share these units with another institution? While mandatory sharing is required in certain situations (i.e., merchant locations) in the statutes of various states, some retailers may also require some types of sharing for their locations. In the absence of a sharing constraint, a bank may find that a regulated MET or POS arrangement can be quite valuable. However, the required investment by a single bank for such a system may preclude consideration of such arrangements by all but the large institutions.

Though the investment is clearly much lower on a shared ATM project, a bank should be particularly careful when considering shared arrangements for off-premise ATM installations. Of course, the exception here is a sharing arrangement with affiliate holding company banks.

The reason why a close look at nonaffiliates sharing is required is that, in terms of a systems approach, the location of such an ATM in, say, a shopping mall or employment center must be made relative to the bank's existing distribution of business and its particular objectives. Therefore, what clearly may be an optimal ATM location for one institution may not be the case for another.

Although much remains to be settled and seen regarding the development of EFTS in this country, we are increasingly able to foresee its impact on traditional branch operations. One general trend regarding these operations in the age of EFTS will be the continued automation of routine transactions that account for much lobby space today. While the branch mean less space for teller windows, counter space, and forms area, it also means more area for other services in which banks may become more active. For example, increased personal financial services and financial counseling by banks is generally expected. Overall, the office space for the average office may decrease and become more efficient in this type of scenario.

EFTS does not mean a branchless society.

In this scheme, a traditional full-service branch acts as a primary hub to electronic service units and limited facilities. These limited facilities, in turn, act as secondary hubs for additional electronic service units. The placement of traditional service units within a given area following this strategy is a function of the major focal points in a region. These offices (particularly the full-service ones) will handle all types of financial transactions, but will focus on those specialized or "shopping" type transactions (say, certain types of loans and counseling) that may be required on an infrequent basis. Commercial and routine activities, such as deposit transactions and some loans, will be primarily handled by the electronic service units.

A bank with a large branching system in an urban area would probably have to close or relocate...
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some branches and scale down others (to limited facilities) in order to accommodate this concept. However, banks and holding companies in certain states that are in the formative stage of branch development (i.e., Florida) are in a position now to evaluate which branches or offices would ultimately function as primary or secondary hubs. The decision to establish full-service branches in areas within a reasonably close distance to other existing or proposed full-service offices of the bank or the holding company affiliates might be reevaluated in this regard.

The possibility that some full-service branches might ultimately be relocated or converted to limited ones indicates the advisability of carefully reviewing the extent of the capital outlay and branch design in branching plans. Also, the purchasing and/or long-term leasing of traditional branches and the construction of an office with little internal flexibility should also be closely examined in this light. Furthermore, the strategy of applying a traditional facility to the hubs for smaller facilities or electronic service units in a given area emphasizes the key role well-qualified branch personnel will play in the system in the future.

What One Study Found

A brief description of a pilot study, which resulted in an optimal five-year service unit strategy for one institution, demonstrates the application of this hub concept.

Although a much broader geographical area was considered as part of the total analysis, one particular market segment was focused upon which was marked quite favorably in terms of its potential. This particular market segment was in a non-SFSA area where the institution had not existing representation. The traditional branching strategy which might be dictated for each market segment would have been the establishment of two full-service branches during the planning period. However, the optimal service units based upon the mathematical programming routine was determined to be one full-service facility within the CBD of the core municipality, which would act as a hub for two electronic service units. One full-function ATM was recommended for a particular location in an existing shopping mall, while another was recommended for the student union at a local university.

Specific timing recommendations called for the initial establishment of the branch facility to create a satisfactory degree of awareness of the institution prior to the electronic service unit entries. It was also recommended that the institution consider the possibilities of a limited POS arrangement with a certain supermarket chain in the area whose store network complemented the institution's proposed service strategy well.

With a much more modest investment than would traditionally be the case, the potential of this particular market segment would still be obtained. Consequently, the resultant profits and return on investment to the institution would be that much greater.

Coping with the Age of BFTS

The importance of a systems approach with respect to branching and electronic service unit strategy in the age of BFTS cannot be stressed too much. As new competitive facilities and service units are established, and you can be absolutely sure they will be, a bank's service unit strategy must be viewed as a carefully thought out branching plan. And a plan of action, rather than one of reaction, is the key to profitable branch expansion.

The Bankers Magazine was first published in 1946 as The Bankers Magazine and State Financial Register. The present title was adopted in 1954. The Bankers Magazine is the oldest American banking periodical. We concede the privilege of our first publisher, Lewis Smith, speaker, who was honored for producing the "true work relating to finance and banking in the Union."