Financial Managers Society

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Second of two parts

Pricing levers for time deposits: strategy

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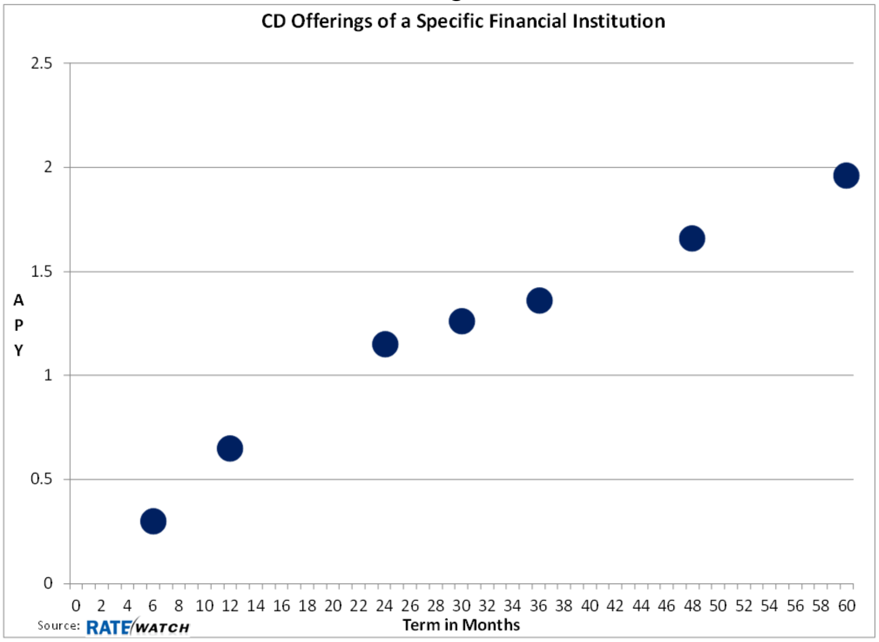
Enhanced control of pricing contributes to achieving an institution's paradise--more profit with less risk. In Part 1 of this series, we described a four-stage sales process that gives pricing managers four levers to control. To better use these levers of control, we will outline here how pricing managers adjust pricing to provide the optimal results for their scenario.

Figure 1 shows the offerings of a specific financial institution before using an enhanced pricing process. Standard offerings are represented by the dark circles ●.

Figure 1 – Before Enhanced Pricing Controls



With a defined consultative Concierge-style sales process described in Part 1 of this series, the process graduates depositors to fresh combinations of service and value as new prices are offered. Without these additional pricing options, fear of the potential reactions from the vocal minority often determines where deposit pricing is set for everyone. An enhanced pricing process helps institutions better serve more people and make more money by differentiating pricing. This allows depositors to make choices which reflect their personal priorities as the sales process progresses.

Four Pricing Levers

Through a four-stage sales process, institutions expand the number of pricing controls. With these four pricing levers they can more simply and effectively address the differing behaviors of the generally silent majority and the vocal minority. Potential pricing for these enhanced processes and products is presented in Figure 2. We now represent the former standard CD offerings in gray to contrast with the pricing of the new offerings in dark blue.

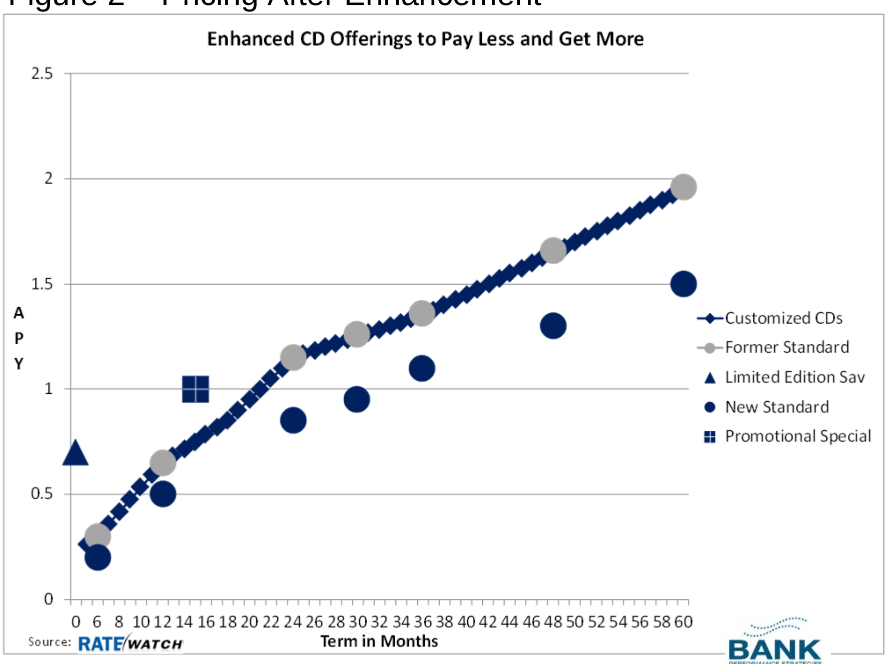
Standard Rates – These are the offerings for standard terms promoted to all customers who are interested. These rates represent pricing typically accepted by the silent majority who most value convenience and simplicity. These are the "express lane" prices that are most favorable to the bank.

Promotional Specials – These are the selectively used offerings publically promoted for their attractive features. This pricing is designed to win new business. Institutions use promotional specials offensively to get noticed. These are always set up to renew as standard term CDs with standard rates at the time of renewal.

Customized CDs – These are privately negotiated offerings for preferred customers. These are used to de-commoditize the sale and defensively address the concerns of the vocal minority.

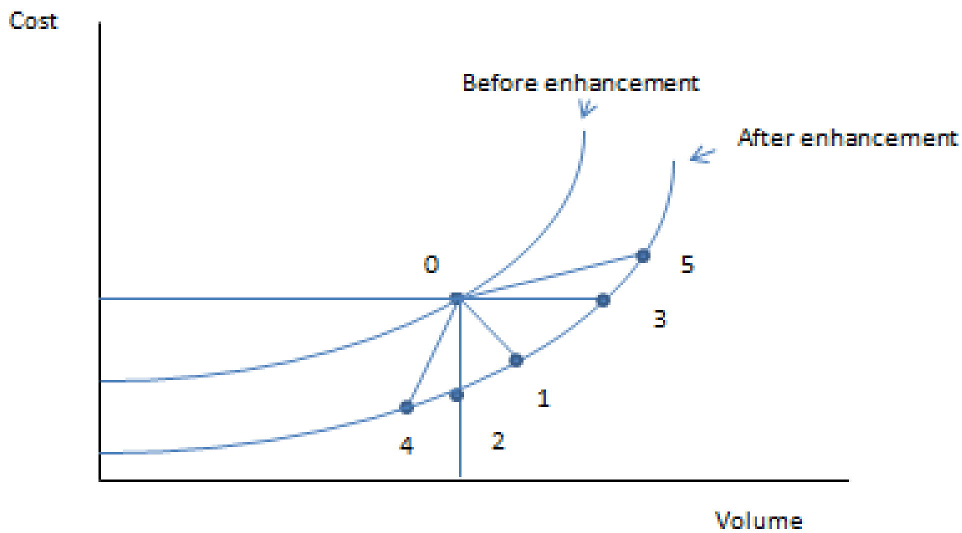
Limited Edition Savings – These are privately negotiated offerings for current CD customers who will leave unless we match competition. These are used to satisfy the obviously dissatisfied holder of a matured CD, without having to match a competitor's higher rate. This is the last line of defense.

Figure 2 – Pricing After Enhancement



This enhanced approach to pricing consistently improves the combination of deposit volume and price paid. See Figure 3.   If the institution had been attracting the deposits at the cost/volume combination noted by point "0", the enhancement would allow the financial institution to shift the supply of deposits enabling the bank to get an enhanced combination of volume and cost. The typical result is paying less and getting more – represented by point "1".

Figure 3 – Relationship between Cost and Volume of Deposits



Once the system is developed to enhance the combination of volume and cost, the financial institution has the opportunity to manage by scenario. To pay less and get more, the financial institution sets pricing generally represented by Figure 2. The institution lowers their standard rates compared to their unenhanced approach; they raise promotional special attractiveness to depositors; they install customized CDs close to or a bit above their former standard CD; and they create Limited Edition Savings at a rate comparable to the blended cost of all recently new and renewed CDs.

Adjusting the Levers

Funding goals evolve over time for every institution. Financial intermediaries constantly search for the lowest cost for the currently required volumes. To adjust for the needs of the institution, pricing can then be refined compared to the initial pay less and get more scenario.

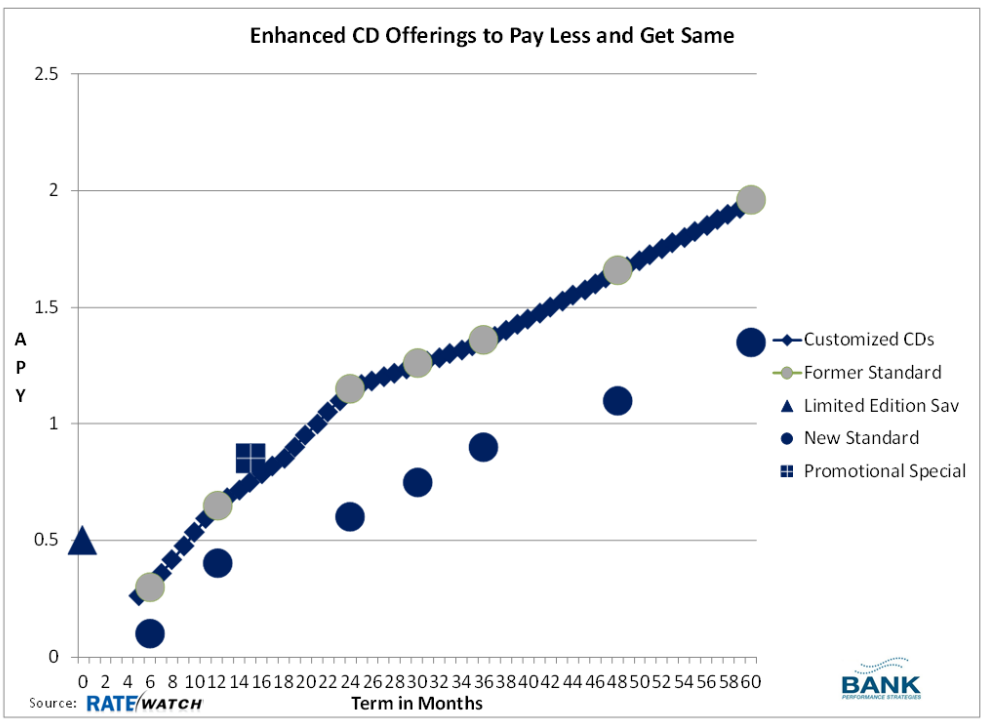
Table 1 – Pricing Adjustments Compared to Enhanced Pricing Position "1" - Pay Less and Get More

Scenario	Standard	Promotion Special	Customized CD	Limited Edition Savings
2. Pay less and get same	Lower	Lower	Lower	
3. Pay same and get more		Raise	Raise	Raise
4. Pay less and get less	Lower	Lower	Lower	Lower
5. Pay more and get more		Raise	Raise	Raise

Adjusting for Profitability Emphasis

When improving profitability becomes the primary focus, the institution will optimally lower rates while minimizing volume impacts. This will typically lead to greater reductions in standard rates; less frequent use of aggressive promotional specials; customized CD and Limited Edition Savings priced just high enough to retain the volumes required. Positions 2 and 4 represent potential cost/volume relationships that can result from these initiatives. The magnitude of the adjustments will determine the specific volume result. Compare Figure 4 with Figure 2 and you will notice in Figure 4 the reduced rates on standard, promotional specials, and Limited Edition Savings.

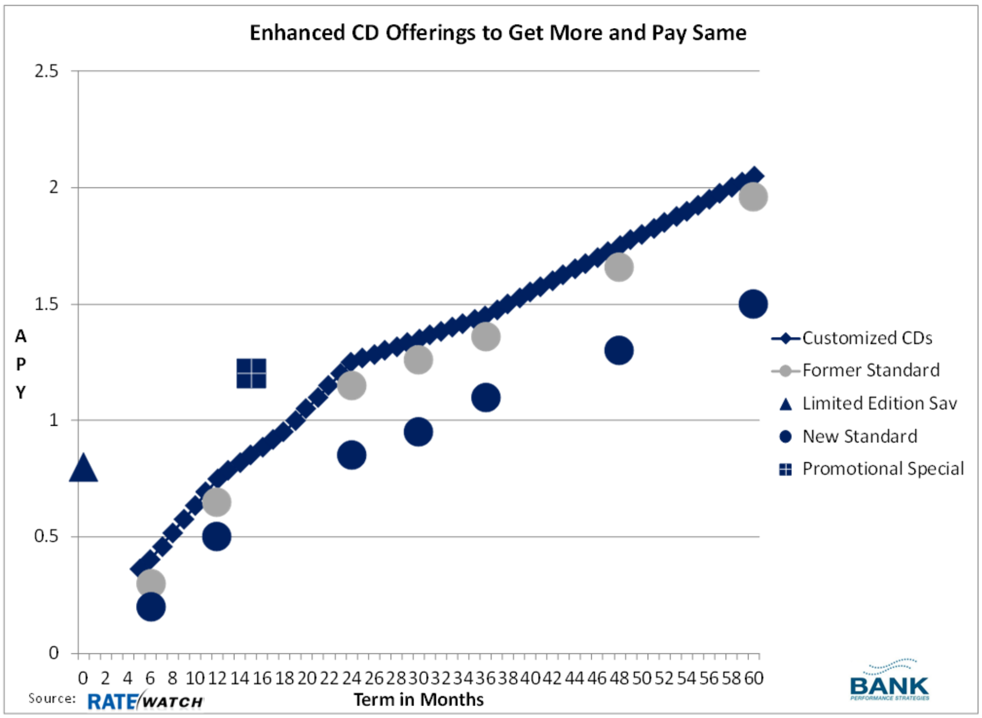
Figure 4 – After Enhancement with Emphasis on Profitability



Adjusting for Growth Emphasis

When the institution shifts its primary focus toward growth, it will seek to attract new funds at the least cost required while minimizing attrition of existing deposits. This will typically lead to more moderate reductions in standard rates; more frequent use of aggressive promotional specials; and customized CDs and Limited Edition Savings priced high enough to be quite confident that deposits will not leave. Positions 3 and 5 represent potential cost/volume relationships that can result from these initiatives. As when the focus is profitability, the magnitude of the adjustments will determine the specific volume result. Compare Figure 5 with Figure 2 and you will notice in Figure 5 the increased rates on promotional specials, customized CDs, and Limited Edition Savings.

Figure 5 – After Enhancement with Emphasis on Growth



Whether you are seeking to purge deposits, hold volumes steady, or grow aggressively, the use of these pricing control levers will give you a much more robust and effective process, typically saving 10-40 basis points of CD interest expense.

In addition to profitability improvement, front-line staffer enthusiasm grows as they are elevated to a concierge level of service - equipped and empowered with tools to deal effectively with the silent majority and vocal minority.

Your pricing options shouldn't require you to have to choose between making more money and growing your business. Use these pricing levers to enjoy the combination of results that are best for your situation and experience more of the banker's paradise – more profit with less risk.

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