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Learning The 'A,B&E's' Of Membership; Little Differences Can Mean Big Results

"Eighty nine percent of members with a checking account write checks. What in the world do the other 11% do? "
–Robert Lawhead

By Frank J. Diekmann, *Editor*

LAS VEGAS–The difference between an "A" and an "E" is a lot more than just five letters in the alphabet. It is often the difference between a thriving credit union and one that is stagnant.

In this case "A" and "E" refer to member profitability as classified by Raddon Financial Group, and while it may seem obvious that it is the percentage of members in each category that drive the credit union's bottom line, less obvious is how small differences can have a large effect on performance.

Robert Lawhead, president of Raddon Financial, told the California/Nevada leagues' annual meeting that the key to profitability is one-to-one marketing.

"One-to-one marketing is nothing more than better member segmentation," he said. "I want you to imagine that on every one of your members you have profitability data."

Lawhead's firm has created five segments, "A" through "E," with "A" the most profitable member. "In our program, one out of every three members are profitable, and 33% of members generate almost three and a half times what you make," he explained. "If you had that information, what would you do with it? Well, first, you better keep those people. When you think of one-to-one marketing I want you to think of getting more participants in the credit union. This is a co-op. You know what I worry about? I walk into your lobby and see three people in line and that third person is your profitable one. I also want to know what the issues are with the other two. It's hard to complain about the 67%, because you gave them the product."

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Raddon Financial has found in its work that typically a credit union's membership breaks down this way: 9% are "A" households (more than $500 profit); 14% are "B;"10% are "C;" 36% are "D," and 31% are "E."

Earning A 'D' On Households

"When we go out and do consumer research, we target the "D" households," he said. "They don't understand you. They say, 'I sold that car five years ago, I don't know why they keep sending me a statement.' The reason is they had to open a $5 share account. That is a typical "D" household. They don't know they're members even though you count them every month.

The 31% of members who are most unprofitable (E), said Lawhead, know very well that they are members. "They cherry pick services among providers. You've got to cross-sell, you've got to one-to-one market those E households," he stressed. "Find some form of segmentation you are comfortable with. Any form of segmentation is better than no form of segmentation. A lot of small credit unions say, 'It's not that big a deal, I've only got 4,000 members, I'll mail to everyone.' What you're doing is educating *all* your members not to read your mail. You've got to get the right information to the right members at the right time. I don't care what size your credit union is; it's only a small number generating profits. A lot of board members will tell me, we need to get more members. I say you don't need more members, you need to do a better job of targeting.' Lawhead stressed he values the cooperative nature of credit unions and that he isn't advocating getting rid of members. Rather, he said, he wants to motivate more members to participate in the co-op.

What separates the "A" household from the "E?" According to Lawhead, the first thing most credit unions point to is that the most profitable households have the most services, yet the “E” households have almost as many services as the “As.” “We used to think that services-per-household was a great indicator,” he observed. “Folks, there is no correlation between services per household and profitability.”

Balances Are What Matter

Instead, the real indicators are balances, according to Lawhead. “What really matters is those balances,” he said. “The E households buy almost as many services, but they don’t bring the balances. You can’t afford the zero-balance household.”

Lawhead said he really doesn’t care what CD rate is given to the A households, as the business they bring more than covers the cost. The bigger question is what to do with the member with the $5 share who wants to deposit $80,000 into a CD, and the bank up the street is offering 50 basis points more. Many credit unions don’t want to let the money go, even though it’s of no benefit to the credit union, he noted, adding that others have been allowing that money to exit, “and the world hasn’t ended.”

“(Alan) Greenspan has done you a world of favors,” said Lawhead. “He has really helped you manage your cost of funds. You don’t have to pay anything. What happens when rates go back up. You’re going to reprice your portfolio. If you get nothing out of this session, go back to your credit union and get yourself a new money market account ready for release. When your CFO says you’ve got to raise rates, your not going to do it on the funds you have. You’re going to do it on new money for those who want to move money into your new account. Will others move their money away? A very small percentage will. You’ve got to think of strategies to bring in new funds at a lower cost, so you can pay rates to the members who are really particiapting.”

What Should Cause Lost Sleep

Lawhead said Raddon Financial has found that households that are costing the credit union more than $100 per year are those with a low loan balance and a low rate. “You can’t lose sleep over low balances. What you lose sleep over is worrying when that member gets a new car, are you going to get the loan? You want their next car loan. You tell them they are a valuable member and they are pre-qualified for their next loan. The consumer doesn’t know the difference between pre-qualified and preapproved. You know what happens after you book most auto loans? You forget them. CFOs tell me the average duration of an auto loan is 32 to 36 months. What do we do? We send the member a letter in the 42nd month?”

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>
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Lawhead said the goal isn’t to turn every “E” household into an “A” household. “You don’t have to make them “A” households, you just have to make them “C” households so that they cover the burden (of their membership),” he explained. “The biggest difference with the high-performing credit unions is they have fewer “E” households.”

In determining the value of households, having activity reports on checking accounts isn’t enough, said Lawhead. That information must be integrated into other data for a more complete picture. “Every checking account has a unique cost based on how the member uses your delivery channels. Every checking account has unique non-interest income depending on fees and interchange income. That checking account with no balances can suddenly look pretty good.

CUJ Resources

For more information on Robert Lawhead or Raddon Financial Group, visit www.raddon.com, or call 800-827-3500.

Four Steps To Take

Lawhead urged CUs to take four steps:

1. Identify dormant checking accounts.
2. Increase bill pay use. “This should be your No. 1 goal right now. Credit unions tell me that’s very expensive. So we allocated the bill-pay expenses only to the households that use it. They were “A” and “B” households before assigning the cost and are “A” and “B” households afterward. They are your most profitable members and they cover the cost.”
3. Increase debit card interchange income. “You have to incent these users. Why? Debit card users buy more loans, and you’re in the business to make more loans.”
4. Increase direct deposit use.

Where is the most cross-sell profitability to be found? Households that use PC-banking. Why? They buy more loans. “They buy the business we’re in,” he noted.

And what is the second most profitable household? NSFs. “Do you have any idea how much you love NSFers? NSFers are great. Do you have any idea why? This is unique to credit unions; we don’t see this in the community banks. Five out of every eight NSFs are accidental. If you don’t have courtesy pay, implement it next Monday morning. That’s why it works so well in credit unions. The NSF households are most profitable. The more NSFs a household has, the more loans we give them. On the other side of the street they won’t even talk to the NSF about loans.”

Thoughts On CRM

Lawhead added, “You can’t talk about one-to-one marketing without mentioning this beautiful term, CRM. Folks, it’s hard to find a lot of success with CRM. CRM is not technology. It is a place we want to go where we bring information to the point of sale or the point of service. If you don’t have the CRM information, you’re going to be looking at the wrong end of a very expensive household. Many credit unions start out with member relationship packages because that’s the way the data processor set it up. Husbands and wives, for instance, are put in different packages. Relationships must be built around the household.”