To guide a more effective outreach to small business customers, progressive banks start with an analytical understanding of customer relationships and behaviors.

As banks continue to scour for revenue growth in a tight market, renewed attention is being paid to the small business market segment, particularly in the area of fee-based services. But while the growth potential is significant, the complexities of marketing, sales and distribution threaten to limit the opportunity for many banks.

One issue is that company size is not always a good predictor of sales potential, posing the risk of over-emphasizing the largest prospects while missing stronger pockets of demand among smaller outfits. Another issue is coping with the diversity of a vast client base that ranges from manufacturing to retailing to service industries.

In threading this maze, banks variously consider the overlapping domains of sales management, relationship management and distribution management. But the trouble lies in doing so cohesively. Too often, incremental improvements still result in a cumulative failure to lift sales productivity and revenue growth in small business banking.

The client development model overcomes this limitation by unifying efforts via an analytical understanding of customer relationships and behaviors. A clear view of the untapped potential with established clients and prospects helps the bank to do a much better job of setting sales priorities. An understanding of which clients want high-touch service and which do not helps to refine strategies for “relationship” versus “transactional” buyers. And a firm grasp of channel usage patterns and preferences helps the bank to take fuller advantage of remote channels to boost revenues and lower costs.

The foundation is a behavioral segmentation based on a profile of each customer, including usage of bank products, services and channels; profit potential; relationship orientation; and value orientation (e.g. price sensitive or utility driven). Translating these customer profiles into actionable segments is the heart of the client development model.
The science of “letting customer information drive strategy” is prevalent in retail banking. The concept is ripe for application in small business banking as well, given the high count of the customer base and the need for precision outreach to optimize sales productivity, customer relationship profitability and channel strategy. This is a much more effective way to market the more sophisticated capabilities of commercial banking within the tiers of smaller companies.

**CASTING THE NET**

Although the U.S. economy is showing more of a pulse, retail banking is still battling the constraints of low demand, low margins and lowered fee revenues. To help offset the revenue gap, banks are expanding their outreach to small businesses, particularly fee-based services.

While the collective opportunity is large, it is fractionated over a large and diverse customer base. Nationally, there are nearly 160,000 small businesses with annual sales of $10 million to $50 million, plus another roughly 1.25 million companies with sales of less than $10 million down to $1 million. This introduces some significant challenges.

The first is balancing profit potential against the cost to serve. Facing higher coverage requirements and lower sales potential per customer, small business bankers have to manage their time quite carefully and can only justify in-depth relationship management with the highest priority clients.

Small businesses also represent a broad array of industry sectors and have diverse profiles and needs. The needs of a $1 million sole proprietorship are different from those of a $10 million corporation. And even companies of the same size in the same industry may operate at far different levels of financial sophistication. Any model that tries to treat all small businesses the same will achieve inconsistent results (Figure 1).

Novantas research also underscores the rising importance of alternative channels in marketing and sales. Survey respondents express high receptivity to sales offers coming from sources other than relationship managers and product specialists. These include telephone and e-mail contact and even suggestions from customer service personnel. These emerging preferences spell opportunity but also vary by segment.

**Figure 1: Evolution of the Small Business Client Outreach**

The client development model improves on prior approaches with an analytical understanding of multi-channel client behaviors and a focus on growing share of wallet.
To illustrate the range of needs across small businesses, consider three typical companies drawn from our market research:

- “Acme Electrical Switches” manufactures specialty electrical components for aviation, marine and automotive applications. Its clients are makers of high-performance aircraft, speedboats and race cars in the U.S. and Europe, and suppliers are in Korea, Taiwan and Singapore. Acme has 40 employees in a high-tech factory and offers a full range of employee benefits including a 401(k) plan. Annual sales are $8 million, growing 20% per year. Their new chief financial officer has experience working at larger companies and is making fuller use of financial products such as letters of credit, foreign exchange, multi-currency accounts, liquidity management tools and a full range of payment and collection services. Acme traditionally financed growth through a combination of revolving lines, equipment finance and commercial mortgages, but is looking for outside investors and has asked its bank for capital markets advice.

- “Redbrick Enterprises” manages suburban office buildings in a major metro market for local investors. It also has revenues of $8 million per year, but there has been little growth since the last development was completed in 2007. Redbrick is family owned. Finances are handled by a family member with no formal financial training, advised by the company accountant who likes to keep things simple. Redbrick does not own any of the properties that it manages, is debt free and has only basic needs for financial services.

- “Flexible U” is a small chain of fitness facilities employing 100 full- and part-time staff, with revenues of $8 million per year. A full-time controller manages day-to-day financial activities with the assistance of a full-time bookkeeper, but the owner is the final decision maker for all things financial and signs every check. The chain has very little debt — occasionally borrowing to purchase exercise equipment or to refurbish rented space — and modest growth ambitions. It uses a variety of basic financial services, including third-party merchant and payroll services.

Of these companies, only Flexible U has the characteristics of a “typical” $8 million company served by a small business banker. Acme has the needs of a much larger company, and would be better served by a relationship manager who can coordinate the delivery of an array of bank services. And although Redbrick’s revenues would typically qualify it for a dedicated business banker, its primary banking interaction is to deposit rent checks at the beginning of the month and write checks for expenses. A bank trying to serve all three

Three-Tiered Market Coverage

The practicalities of running a business require some level of segmentation based on size, especially when dealing with prospects or as a way of aligning business banking with the retail network. This calls for a three-tiered organizational construct.

Branch managers typically form the front line of small business banking, and they are usually the primary bankers for the smallest companies, generally those under $1 million in sales. Because they must handle the needs of consumers as well as businesses, branch managers rarely have the time, or the requisite skills, for in-depth relationship management. They are, however, often the first contact that clients have with the bank, and they open many business accounts. Without support, they are unlikely to be effective at client development.

Small business bankers are dedicated business specialists charged with developing client potential. Although some banks assign SBB’s to companies as small as $250,000 in sales, it is difficult for the specialists to justify much time with clients having less than $1 million to $2 million in sales. Even when focusing on larger customers, they usually are spread thin and can usually provide only basic relationship management support. Effective prioritization and targeting are essential for their success. Many banks are finding that remote small business bankers — working with clients by phone — can be a cost effective alternative to in-market SBB’s.

Business banking relationship managers can provide a more intensive level of engagement with larger clients having the needs and revenue potential that justify the effort. Typically this would be companies with at least $10 million in annual sales. Business banking relationship managers serving this segment can be expected to engage in true relationship management, including account planning and coordination of specialist sales teams from treasury management, merchant services, specialty lending and capital markets.

Within each organizational tier, behavioral segmentation drives the client development model. In some cases, clients may be reassigned to a different tier that is better aligned with their behavioral characteristics.
companies with the same model would miss opportunities with Acme and devote too many resources to Redbrick.

**BEHAVIORAL SEGMENTATION**

To be sure, experienced small business bankers are aware of the diversity of the customer base, and some organizations and calling officers have honed their marketing and sales techniques to outdistance competitors. There is still a lot of leakage, however, even among top competitors in this space, with myriad opportunities lost as organizations expend their energies in the wrong directions.

A major reason for such disappointments is that many banks have not yet learned to capture the distilled guidance that comes from a more scientific analysis of the full small business customer base. While a side-by-side behavioral analysis of hundreds or thousands of clients may have been less feasible in prior eras of banking, that level of sophistication is now a reality — and rapidly becoming a competitive requirement.

Behavioral segmentation provides an analytical foundation for a targeted client development model. It begins by profiling the customer portfolio to quantify the value and potential of customer relationships and determine key success levers. It builds on these profiles by creating discrete behavioral segments within the portfolio. And it uses segmentation to drive resource allocation and client development approaches to achieve desired results, such as increased share of wallet or retention of profitable customers.

Customer profiles are based on a variety of factors, including current usage of bank services, profit potential, relationship orientation (e.g., transactional vs. relational) and value orientation (e.g., price sensitive or utility driven). Many factors, such as usage trends and price sensitivity, can be assessed based on balance and transactional history. Share of wallet analytics can provide an estimate of untapped potential. Insights into relationship orientation and price vs. utility trade-offs can be gleaned from bankers’ calling notes and histories stored in customer relationship management databases.

In most cases, this information should be used to derive a forced segmentation based on a hierarchical series of factors used to categorize the portfolio into discrete customer groups. Each behavioral segment should be aligned with a concrete development objective. In one approach, for example:

1. The first factor is profit potential. Clients that promise the most overall potential, as measured by annual margin, lifetime relationship value, or some other appropriate metric, should command the greatest share of resources. Note that the clients with the greatest potential may not be those that are currently the best, most profitable customers. Banks should focus on developing the untapped potential of customers if they want to achieve growth in a tough competitive environment.

2. Relationship orientation is another factor. Although banks may aspire to nurture deep client relationships, not all clients are interested. Clients who view banks as purveyors of financial commodities demand different treatment from those who are relationship oriented. To serve these “transactional” buyers, the bank needs an adaptable client development model. One size does not fit all.

3. Third, an analysis of current usage helps to define the objectives of client development. For example, retention should be the objective for profitable customers with whom the bank already has a high share of wallet. For single-product clients, the goal is cross-sell. In other instances, re-pricing may be an effective approach for clients that use a full-range of services but produce mediocre margins. Of course, for high-potential prospects in attractive markets, the goal is acquisition.

Once all clients are aligned with an actionable segment, the key to success is execution. This includes sales strategy; targeting the right offers to fully develop the potential for clients in each segment. It also includes channel strategy; reaching customers through all touch points including the direct sales force, inside sales, online channels, the external website, service-to-sales and advertising. Then with sales force design, the bank refines organizational structure (specialization, roles, reporting, responsibilities), deployment (coverage, resource levels) and performance management (metrics, compensation, incentives, training).

**THREE FACTORS**

There are three factors that will boost the organization’s effectiveness as it puts these concepts to work in small business banking. These include using customer analytics to generate...
The Client Development Model for Small Business Banking

Targeted Leads. This is essentially an extension of the same behavioral analysis that is used to segment the client base. Here the analysis is used to identify opportunities to introduce clients to new products and services, consistent with their financial needs and financial management capabilities. Novantas finds that a behaviorally targeted approach can generate from three to six times the number of leads that typically can be identified by an over-extended business banker or branch manager.

Inside Sales. A dedicated team of sales professionals, interacting with clients by phone, can be highly productive in handling the large number of leads generated by behavioral analytics. The inside sales force will complement the efforts of branch managers and local business bankers, or even act as primary bankers for some client segments. Novantas research has shown that an inside sales unit can contact clients and close deals at one-half to one-third the cost per sale of a field sales force. This not only reduces the cost of sales coverage, but also makes it feasible to manage and cross-sell clients that would otherwise be unprofitable or simply neglected.

Online Fulfillment. Many sales are lost because of errors, delays or miscommunications in implementation. With large commercial clients, support staff can manage the process of underwriting and booking loans, or implementing cash management services. But this model is simply too costly for small business clients, so most banks rely on branch managers and business bankers to “get the paperwork right” and manage the onboarding process — a recipe for miscommunication and human error.

A more effective approach uses online tools to make the onboarding process highly automated and much more transparent. Simple services can be activated by simply clicking a button in the online banking system. More complicated processes, such as loan underwriting, can be tracked online, by the primary banker and the client. Meanwhile so-called “e-sign enrollment” eliminates the need for most paper documents.

Not only will the client development model help banks achieve growth in a challenging market, but it will also lead to more satisfied small business customers. According to a 2012 survey of small businesses by Novantas and Greenwich Associates, the most important attribute buyers look for in their banker is someone who “understands the needs of my business.” What better way to make clients and prospects happy than to arm their bankers with behavioral insights so they can do just that.

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Vertical Segmentation

So called “vertical segmentation” has logical appeal, and the idea is to provide market coverage arrangements that are customized for companies in various industry sectors (healthcare, retailing, construction, etc.) However, cost constraints limit the feasibility of this approach in small business banking.

For one thing, the comparatively lower revenue potential per client makes it difficult to justify the development of industry-specific products. Also the client base tends to be widely dispersed geographically, making it expensive to deploy an industry-specialized sales force.

Yet a vertical segment strategy is warranted in certain cases. For example, high sector concentrations in key markets (e.g. non-profits in Washington, D.C.; high-tech companies in Silicon Valley; entertainment companies in Los Angeles) can mitigate the typical challenges of serving a dispersed clientele. A bank may be in a position to build on an already strong competitive position to “own” an important segment.

Cost effective vertical segmentation requires efficient use of resources. Some customer segments have a higher propensity to use specific banking products, which can be bundled into targeted offerings. Examples include:

- Retailers — merchant services; inventory finance; sales tax payments, coin & currency.
- Healthcare Practices — equipment finance; liquidity management; merchant services.
- Law Firms — Interest on lawyer and trust accounts; liquidity management; partner loans, remote deposit capture.
- Manufacturers — cash flow lending; equipment finance; international wires/foreign exchange.

Finally, centrally located industry specialists can support in-market bankers via remote channels (phone, video), making it feasible to maintain sector-specific expertise.