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COMMUNITY BANKING

COMMENT / BY PAUL NADLER

Bottom Line, Accounting Is Not for Accountants Only

A publication from the Association for Management Information in Financial Services makes the case that some community banks fail to turn a profit because of their failure to consider accounting in decision-making.

The main theme of "Keys to Community Bank Success/Utilizing Management Information to Make Informed Decisions," by Robert Kafafian, president of consulting services for Tucker Anthony Sutro Capital Markets, is that management accounting is not just for bean counters.

It can help top-level executives highlight the most/least profitable business lines, products, and customers and point to ways to get the most from the most profitable areas, Mr. Kafafian says.

The 84-page book includes a case study of a bank that appeared to be in such bad shape that the board decided to sell. "Appeared" is the operative word: If the bank had been

more thorough, Mr. Kafafian writes, it would have found that it wasn't going down the tubes — it was headed for profitability.

The book also stresses the importance of knowing fund costs and operating costs to determine whether products are appropriately priced and whether they are loss leaders that perhaps should be discontinued.

Banks typically have "step variable costs" when they operate at excess capacity, the book says. In other words, they have excesses in funds, computer capacity, and employee time, so they wind up taking on business at low rates to use up this excess capacity. Then, when they have used this capacity up, they begin hiring more people and buying new equipment.

Understanding pricing elasticity is another key to profitability, Mr. Kafafian says. If a service costs more than the bank can earn at the price it

feels it can charge, it must try to find out whether a good percentage of customers would be willing to pay more.

Knowing this sort of thing can be a considerable competitive advantage.

Mr. Kafafian also discusses the importance of fee income, but he says spread management still has to be first priority for many community banks in profit-generation, because unlike their larger brethren, they cannot develop lucrative fee-generating products fast enough or without a considerable time lag.

The book is published in the association's *Journal of Bank Cost and Management Accounting* and is available through the group's Web site (www.a.mifs.org).

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