

# Crossing the Balance Sheet

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*Identifying best practices when designing a cross selling initiative between capital and credit market teams.*

White Paper

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## **Crossing the Balance Sheet**

***Measuring best practices when designing a cross selling initiative between capital and credit market teams.***

### ***Executive Summary:***

Competition in the financial services marketplace has created a customer that is more expensive to acquire, much harder to keep, and less profitable when they stay, forcing banks and financial services institutions to rapidly invest in a future based on the effective collaboration of their internal divisions, and their external partnerships. This vision, when fulfilled, should lead to the development of products that meet both the anticipated and unanticipated needs of the customer, expanding the customer's relationship with the institution, while simultaneously increasing the institutions profitability and retention of that customer.

As institutions integrate their vision of this future, independent financial advisors and lending professionals are finding new and creative ways to compete with these deep resources and comprehensive product lines of the financial "superstores", further increasing the marketplace competition. In this paper, we'll explore the past and present institutional definitions when referring to 'cross-selling' initiatives, and compare those to some of the more integrated solutions being proposed for 'cross-balance-sheet' selling now appearing at a grass roots level. In addition, we'll discuss the core actions a institution must take to ensure cross-selling success, as well as specific ways to motivate financial advisors to increase their level of cross-selling when helping their clients meet financial goals. These 'cross-balance-sheet' relationships are binding referral partnerships between such unlikely candidates as mortgage brokers and financial advisors, or insurance agents and Realtors.

### ***How did we end up here?***

Banks and financial services companies have long sought to shed the shackles of the Glass-Steagall Act, which inhibited cross-selling opportunities and limited their long term profitability potential. As regulatory restrictions were slowly being lifted during the 1990's, the United States experienced an unprecedented long-term rally in both the equity and debt markets, delivering record profits to the banking and financial services industry. The recent bear market has left many investors sitting on the sidelines, while many others are heading for the exits. As a result, banks and financial services companies' aspirations for double-digit revenue growth have been supplanted by cost cutting and risk management initiatives designed to stem double-

digit losses: profits at publicly traded NYSE institutions have fallen from \$16.2 Billion in 2000 to \$5.2 Billion in 2002.<sup>1</sup>

Throughout both bull and bear markets, competition in the financial services industry continues to intensify as banks, wire houses, discounters, and other financial services institutions that formerly relied on unique product lineups to attract customers are finding it more difficult to differentiate their offerings from those of their competitors. Independent financial planners and lending professionals are looking for ways to compete with the deep resources and comprehensive product lines of these financial “superstores”. The cost of acquiring customers continues to rise, and margins continue to be squeezed as differentiation becomes more elusive. To fully compete, institutions must become more aware of the changing landscape of the consumer market, and what they consider a real value.

### ***The Changing Landscape***

Throughout the '90s, financial planning topics became increasingly popular in the United States. The news media repeatedly reminded baby boomers that they weren't adequately prepared for retirement, creating a wave of concerned customers looking for financial advice. The financial services industry responded with a host of new services and competitors chasing this demand, from deep-discount Internet brokerages and day-traders to high-end full-service boutiques. With the passing of the Gramm Leach Bliley Act in 1999, Congress tore down the walls separating bankers from insurers and Wall Street institutions, adding fuel to the competitive fire. This action, combined with pressure for greater disclosure requirements, has resulted in fierce downward margin pressure among financial services players.

As the bull market peaked, investors came to expect 20% yearly returns on their investments and projected out a bold new retirement expectation based on the impact this compounding would have on the growth of their savings. Seeing no benefit to a long-term advisor relationship and heeding the call for “diversification” among service providers, customers spread their investments across a dozen no-load mutual funds and/or a handful of brokerage accounts. As the assets spread thin, full-service investment institutions struggled to manage the cost of maintaining accounts. While individual planners, advisors, and wholesalers were making headlines with their mid-six-figure incomes, behind the scenes their institutions were finding it difficult to contain costs while managing high account turnover and increased trading activity with tighter spreads. All these factors combined to create an environment where customers were more expensive to acquire, harder to keep, and less profitable when they stayed.

Looking for ways to make customers more profitable and loyal, financial services companies continued their efforts to acquire a diversified product line and cross-sell

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<sup>1</sup> Bloomberg Markets, “Wall Street’s New Rules”, May 2003

it to their customers. As financial advisors solicited investors to swap their bank CDs for mutual funds or annuities, banks promoted low cost term insurance in their customer statement stuffers to attract potential investors. For many years, institutions were successful at luring each other's customers away by relying on their unique core product strengths for profitability, and providing low cost, low profit commodity products in the name of 'cross-selling'. The customer has become accustomed to getting services at a discount, and this expectation is now putting price pressure on the institutions core products that were important for long term profitability. A source at GE Capital told us that in the late 90's First Union purchased mortgage servicing based on an expected ratio of selling 6 new products to each mortgage they serviced, but the actual number ended up closer to 1.2. The initial 'cross-selling' value of most relationships seems to fall short in the key areas of per customer profitability, and long term customer retention.

Furthermore, the bulk of cross-selling efforts have remained within the various operational silos of many institutions. For example, a State Farm agent sells life insurance to one of their auto insurance customers. Is this a cross-sell, or an extension of the same product line? Is a Wells Fargo loan officer selling a home equity line to a new home buyer at closing a cross-sell? If a Wachovia Private Customer Services rep converts a CD to a mutual fund, is this the true definition of a cross-sell? The answer, as you may have guessed, is "it depends..." The simple *offering* of these products isn't enough to keep customers from shopping: in many cases it stimulates the customer to shop further as they view each product as a specific commodity available at all institutions. Although these institutions often present a comprehensive product line to their customers, most are not integrating the products at the point of need, in a compelling manner that truly highlights a specific solution to the needs of the customer. In the end, the resulting intra-silo cross-selling fails to tap into the full profit potential of a customer, fails to deliver true value-added service, and most importantly accomplishes little in the way of transforming the traditional, functionally-oriented customer relationship into something substantially more meaningful or beneficial.

To deliver maximum value to customers through cross-selling, and to reap the rewards of stronger customer satisfaction and loyalty that follow, institutions must provide knowledge, tools, and systems to their representatives (such as a financial advisors) to enable them to effectively present these products (such as a mortgage loan) in a manner that is relevant to the customer's specific needs. They also must integrate each product offering into a comprehensive plan that assures the customer that they are the ones making an educated decision relevant to their long term financial and life goals.

### ***Cross-Selling - The Elusive Holy Grail***

Despite the time, effort, and money that the industry has dedicated to improving its cross-selling performance, most institutions continue to struggle at developing their non-traditional product lines. Cross-selling was recently dubbed "the Holy Grail" by

Wachovia CEO Ken Thompson<sup>2</sup> – and it has proven to be just as elusive. With the exception of Merrill Lynch, who originated over \$20 Billion in mortgages in 2002 (roughly \$1.6 million per advisor), traditional financial services companies have struggled to gain critical mass in residential mortgage lending, which is arguably the single-most lucrative cross-selling opportunity from a long-term customer relationship perspective. “It gives you an opportunity to provide a lot of counseling”, says Mark Oman, chairman of the residential mortgage division at Wells Fargo.<sup>3</sup>

For example, Wachovia Securities - a bank-owned financial services company - originated just \$1 Billion in the same calendar year, (roughly \$125,000 per advisor). Even more noteworthy is the fact that Wachovia Securities’ modest results are far superior to many of their brokerage peers. This sluggish performance applies equally well in reverse, as banks have had a similarly difficult time trying to cross sell asset management products to their mortgage and credit customers. A recent study by the Gartner Group found that, while 74 percent of companies say they are cross-selling to customers, 70 to 90 percent of all cross-sale efforts fail.<sup>4</sup> Why is this the case when companies are dedicating so many resources to improving their cross-selling competencies?

## **Why Cross-Selling Fails**

The reason for this failure can be boiled down to three main categories. First, institutions find it difficult to implement cross-selling across traditional business silos. Second, the flow of information is fragmented between the customer, the employee, and the institution, so that these parties are not comprehensively communicating the information that is necessary to enable the institution to optimally help customers reach their financial goals. Third, core corporate policies and support services are not sufficiently developed in a cohesive, integrated manner to best facilitate cross-selling efforts. Each of these issues is discussed in detail below.

## **Isolated Operational Silos**

The operational silos of the past are stubbornly holding their ground. While the cross-selling statistics have improved, individual bankers, agents, and brokers are still sticking to what they know best, and transactions being labeled as cross-selling are in reality nothing more than intra-silo product proliferation. A report by the ABA noted that, “Banks traditionally have not done as much cross-selling with their mortgage customers...because mortgages have come from a different part of the retail bank.”<sup>5</sup> Selling more products to a single customer can be good for the customer and the institution offering the products, but when a product comes from

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<sup>2</sup> G. Kennedy Thompson, speech at UNC Kenan-Flagler Business School, April 1 2003

<sup>3</sup> “Why Wells Likes Mortgages”, Mortgage Banking, June 2002

<sup>4</sup> “Cross-selling software boosts bank marketing”, Bank Marketing International, January 22, 2003

<sup>5</sup> “Cross-Selling to Your Mortgage Customers”, Bank Marketing, January/February 2001

within the same silo of operation, is it a translative (movement of something to another place) offering, or a transformative (changing dramatically in appearance) customer experience?

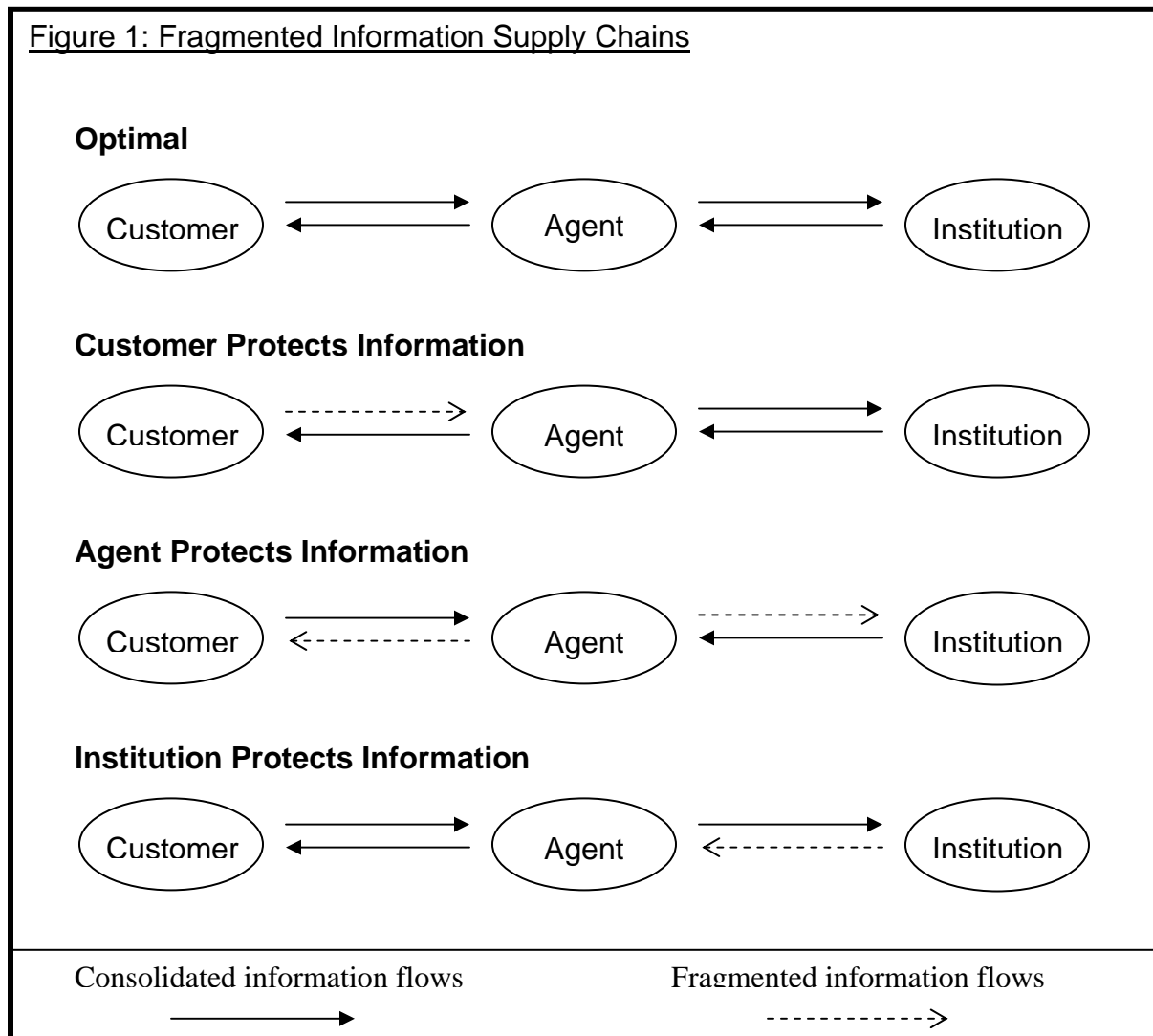
Before developing specific cross-selling initiatives, institutions must first clearly articulate the goal of these initiatives and carefully define the metrics used to measure the results of cross-selling so that these metrics truly reflect the results of the cross-selling in terms of the institution's end goals. For example, many institutions measure cross-selling in terms of the cross-sell ratio of products per customer, establish quotas for their employees, and set bonus targets based on this quantitative measurement. However, by closely monitoring employee activities and pushing for cross-sell productivity, these institutions may inadvertently discourage employees from engaging in customer service activities that don't directly produce a sale. By doing so, institutions create an environment where no employee is motivated to resolve a customer problem when it arises, leading to a decrease in customer satisfaction and loyalty.

Each institution will evaluate the goals of cross-selling uniquely, but must recognize that one homogenous cross-selling strategy does not apply to the full range of intended end goals. For example, if the institution's end goal is to increase customer loyalty and long-term profitability, and cross-selling is the means to this end, both quantitative *and* qualitative measurements must be introduced to ensure that the customer's needs are being met at the level of service quality they expect. Additionally, cross-selling effectiveness should not be measured solely in terms of products per customer, but in terms of providing additional products that specifically address the customer's most timely and critical needs. Making a translative sale, such as selling an IRA account to an investment customer might increase the institution's cross-sell ratio, but it has little impact on the customer relationship> If the customer owns a high-rate mortgage and the institution misses the opportunity to save the customer money through refinancing – a transformative opportunity was missed as the institution could have provided timely and critical value-added financial advice that yields the customer savings that could enhance their likelihood of meeting retirement goals.

### **Fragmented Information Chains**

In recent years manufacturing organizations have dedicated a substantial amount of labor and capital towards improving their supply chains. Although the financial services industry has also worked to improve its supply chain, here the supply chain consists of funds, services, and information rather than physical goods. Inventory sits not in warehouses (traditional supply chain) but in a file cabinet or computer (information chain), in the form of customer information that is not being efficiently distributed to the business silos to make that information productive. In financial services, information typically flows between three entities: the customer, the institution, and the agents who represent the institution while interacting with the customer. This three-way information chain introduces the opportunity for

information to be lost, underutilized, or concealed by any one of the entities, resulting in fragmentation of the information chain. This fragmentation, much like in a manufacturing organization, results in inefficiencies that result in a decrease in customer service levels, unmet customer demand, and lost revenues to the institution. Figure 1 depicts the fragmentation that occurs when one of the members of the information chain protects, loses, or underutilizes information from the other members.



As figure 1 illustrates, fragmentation in the information chain results in the obstruction of information flows to the other members of the chain. When the customer withholds information, the agent and the institution are unable to adequately deliver the advice and optimal financial solutions to meet the customer's needs. When the agent protects, loses, or underutilizes information, the institution fails to acquire information about the customer and as a result fails to deliver optimal solutions in return. For example, the agent might not list the customer's



mortgage rate in the institutional database, thus prohibiting the institution from monitoring rates on the customer's behalf and using technology to identify a refinancing opportunity on a timely basis. Alternatively, the institution might offer special relationship pricing to customers who have their mortgage with the institution, but the agent fails to inform the customer of this savings opportunity for any of several reasons. As a result, the customer is unable to take advantage of this benefit. Finally, when the institution protects or underutilizes information (for example, the mortgage division does not provide client-authorized financial information to the investment division), it constrains the agent's ability to present optimal advice and integrated product solutions to the client. Note that this model depicts only one of many different service delivery models that exist in the industry. Different firms with different models (internet-based, call center based, etc.) will have unique and varying information chains.

There are several reasons that such fragmentation in the information chain can occur. First, geographic barriers may separate the customer from the many independent business silos of the institution. Whereas a mortgage loan officer in a bank branch can walk over to an account manager to obtain a CD rate or open a checking account for the customer, he or she may not be able to meet with an investment advisor who sits in a different office. Geographic barriers result in communication weaknesses that can fragment the information chain.

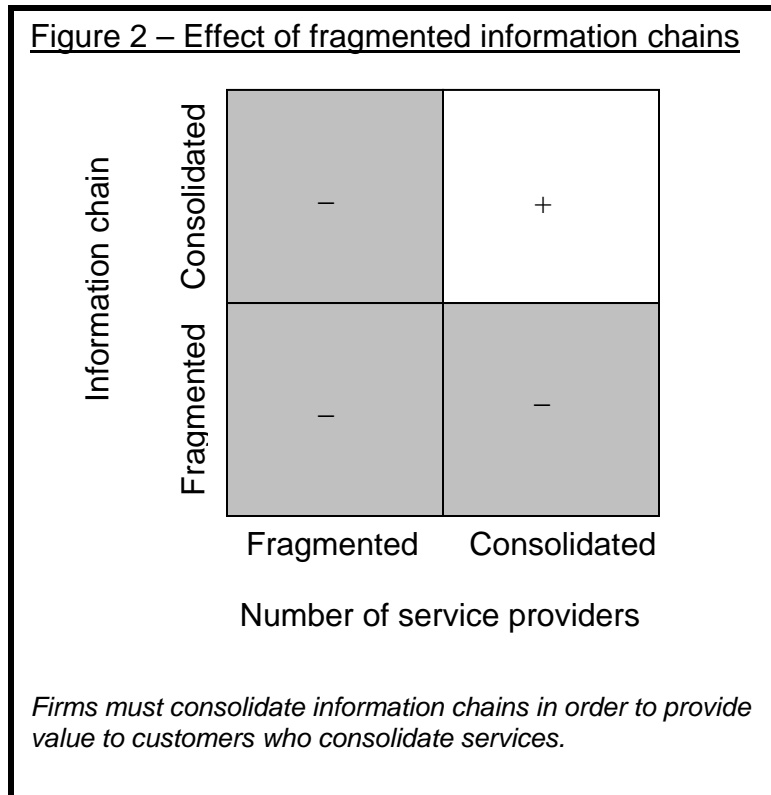
Second, the institution's agent might protect or hoard client information. This might happen because of many reasons that are described below under "the challenge for institutions". Additionally, the agent (such a financial advisor) might feel the need to preserve the independence of his customer relationships. One reason an advisor might do this is to increase the likelihood a customer would follow him if he should ever decide to switch employers. Another source of fragmentation caused by the advisor is when an advisor fails to present products to the client because the compensation for the product conflicts with his personal marketing strategy. In many cases, this attempt by an advisor to hoard customer or institutional information can backfire on him, resulting in an unsatisfied customer who then begins the search for a new financial services provider who can better meet their needs.

Third, business silos within the institution might hoard client information. Again, there are many reasons why this could happen. One might be an incompatibility of legacy systems in various silos that prohibit the transfer of this data. A second possible reason is that a dominant silo in the institution might feel the need to preserve lucrative customer relationships from risks that could arise by introducing the customer to other silos. For example, the investment banking arm of an institution might be reluctant to refer a corporate client to another division because the banking unit fears that its control of the relationship could be diminished through the introduction of new services to the customer. Third, the transfer of information between silos could be fragmented because of "language" barriers – differences in terminology between the silos. In our interview with Randolph J. Cary, President and CEO of Mid-Carolina Bank in Burlington, NC, he noted that his lending officers

“speak their own language” compared to other professionals in the bank.<sup>6</sup> The convergence of the credit and capital markets has necessitated that terms such as “rate” and “qualified” be redefined to encompass a broader range of meaning when loan officers and investment advisors collaborate to address customer needs.

Figure 2 shows the adverse effects of information chain fragmentation. When a financial services institution fails to consolidate information chains internally, the value added to customer relationships diminishes. As a result, the customer finds no benefit from consolidating services with one provider and may find their needs better served by turning to multiple service providers. In this fragmented scenario, all parties are adversely affected.

Fortunately, research has shown that customers prefer to consolidate their services with one provider as long as the services provided are competitive with outside offerings. As a result, institutions remain motivated to improve their information chains, and both parties stand to gain substantial benefit as these information chains consolidate and improve over time. The institutions that can implement improvements fastest will accrue competitive advantages over those that lag.



**Misaligned Policies and Support Services**

In order to achieve success through cross-selling, institutions must align 10 core policies and services with their cross-selling end goals:

1. **Organizational focus** – Executive management must clearly define the institution’s objectives and communicate these objectives to their management teams and their subordinates. Organizational mission, values, and goals must align with the institution’s cross-selling end goals, crossing silos to permeate the organization as a whole.

<sup>6</sup> Interview with Randolph J. Cary, President and CEO of Mid-Carolina bank, 5/15/2003

2. **Organizational and individual performance measurement** – The institution must establish performance measurements that reflect the end goals, not simply means to these goals. They should encourage the flow of information, products, and capital
3. **Compensation Policy** – Management and employees should be compensated based on both quantitative and qualitative performance in congruence with the cross-selling end goals.
4. **Motivation** – Recognition programs and incentives should reward cross-selling in a manner that closely aligns with the end goals.
5. **Procedures** – Institutional procedures should facilitate cross-selling activities and information flows between business groups, or “silos”.
6. **Information technology** – Systems must be established and integrated to facilitate the flow of information, products, and capital between the customer, employee, and the institution, *across business silos*. They must also be structured to accurately measure operating performance comprehensively, and in terms relevant to the institution’s end cross-selling goals.
7. **Service Delivery** – Products and services must be delivered to the customer in a manner that reinforces the type of relationship the institution desires to achieve with the client. For example, if a product is designed to be sold through an advisor, that advisor must be empowered to address any issues that might arise through the sale of that product. Additionally, information channels should be constructed to facilitate the identification and satisfaction of customer needs. As Mr. Cary noted in our interview, the advisor is often faced with the task of resolving differences between the products that the institution is promoting and the products that best address the customer’s unique needs.<sup>7</sup>
8. **Support services** – Support mechanisms and financial resources must be allocated in a manner that enhances cross-selling efforts, and must support the agents or systems that execute the cross-selling strategy across silos within a consolidated information chain.
9. **Product offerings** – Products and services should be designed to deliver integrated financial solutions to customers that address their needs in a comprehensive manner. Customer information should be shared across silos to ensure that product solutions provided by various silos are compatible with each other and are consistent with the client’s overall financial goals.
10. **Pricing policy** – Product and service pricing should reward clients for loyalty across the balance sheet and between silos. A customer with a large lending relationship is equally valuable to the institution as one with a large investing relationship, and such a customer should receive preferred pricing on all services throughout the institution, regardless of the silo within which the largest revenue is generated for the institution.

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<sup>7</sup> Interview with Randolph J. Cary, President and CEO of Mid-Carolina bank, 5/15/2003

## **Crossing the Balance Sheet**

Once an institution has built a strong platform to support its cross-selling initiatives, it must look for ways to sophisticate its cross-selling program in order to forge stronger customer relationships through transformative cross-selling. In this paper, “Crossing the Balance Sheet” describes a sales approach that entails offering combinations of products on both the asset and liability sides of the customer’s balance sheet. This integrated solution to a customer’s needs meets both the anticipated (translative) and unanticipated (transformative) needs of the customer.

Products that are sold across divisional silos might involve selling between two divisions within a single institution, or two separate institutions working in partnership – the challenges are still the same. We believe that true cross-selling must:

- **Add wallet share to the financial institution** – by increasing the income to the financial institution without a disproportionate increase in expense.
- **De-commoditize the offering** – by reducing the likelihood that the customer will view the service as a commodity and thus reduce the relationship rather than extend it when a similar product is offered for less by a competitor (‘gas station effect’).
- **Increase loyalty** – by reducing the likelihood that a customer would risk leaving the relationship for another competitor, as there is much more at stake now for the customer if they leave.
- **Perceptual transformation** – the customer doesn’t view the institution as a vendor, but a financial partner who can meet their needs in their entirety.

To accomplish these goals, aspects of the transaction for the customer must move outside operational silos and *cross the balance sheet* to clearly address both the customer’s asset management and credit management needs in relation to their overall financial life goals.

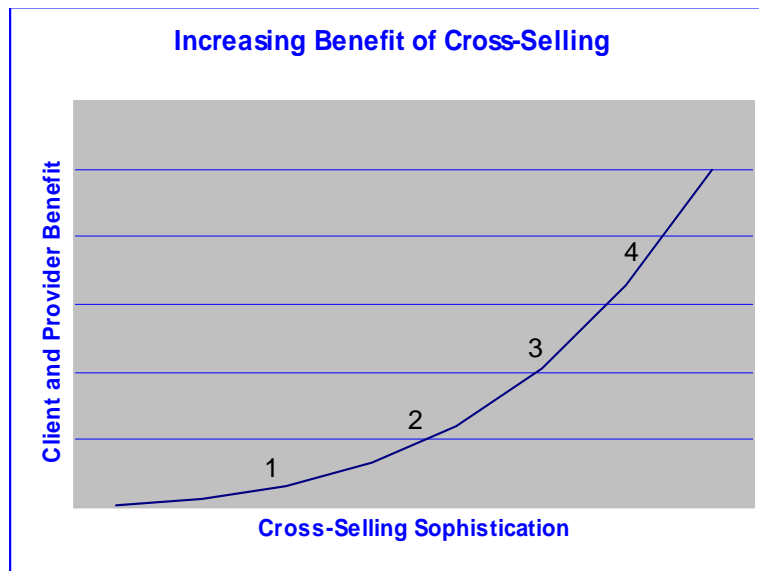
*Example: A refinancing homeowner meets with a loan officer and is encouraged to consider both a 30 year fixed and an interest only mortgage. The loan officer recommends that the customer review the savings created by the interest only mortgage with the bank’s financial advisor. The financial advisor then illustrates how the payment and tax savings from the interest only mortgage could pay for needed life insurance and college savings.*

The customer benefits through the resolution of three problems: a need to reduce their interest rate (anticipated), a need to increase their insurance protection, and a need to begin savings for their children’s college (unanticipated). The perception of the customer is altered through this resolution of identified needs.

## **Four Levels of Cross-Selling**

In the prior example, the institution created a transformative experience for the customer and provided a more complete cross-sell relationship by integrating not only products, but differing levels of expertise provided by the loan officer and the financial advisor. Institutions might consider whether cross-selling is an end goal in itself, or whether the cross-selling is the means to reach a greater goal of increased customer benefit and value. The return a financial institution receives on its cross-selling efforts increases exponentially with the depth of the product impact on the customer, which is in turn a direct result of effort placed on the integration of the product cross-over between the operational divisions. Additional long term cultural changes are created as divisional silos find a way to work together in this process and the organizational structure moves from a pure product orientation to product *and* experience.

**Figure 3 - the customer and provider benefit at various levels of cross-selling.**



- Level 1: Add Wallet Share: Increase the profitability of a customer
- Level 2: 'De-commoditize': Provide value that is highly visible and unique
- Level 3: Increase Loyalty: Improve customer satisfaction and retention
- Level 4: Transform Customer Perception: from product vendor to 'financial partner'

To further illustrate figure 3, we'll discuss each level of cross-selling in greater detail:

### **Level 1: Wallet Share**

'Intra-silo' Cross-Sell: A customer is being sold a home equity line of credit with their mortgage. The customer's initial motivation for doing business with the institution might encompass convenience (due to the existing relationship) and transaction cost savings (price). We would consider this a Level 1 'intra-silo' cross-sell.

To move this customer beyond Level 1 we must ask:

- *How does the customer know they chose the best mortgage for their needs? Was this clear to them at the close of the transaction?*
- *Was the product choice part of something larger than the individual product decision? Is there an emotional benefit being provided?*
- *Were the savings and benefits highly visible?*
- *Was the ultimate product sale a commodity that could decrease customer satisfaction if they viewed the same product offering from a competing bank at a lower price the following day?*
- *Did the integration of the cross-sell initiative lead to a relationship that would be difficult to recreate by a competitor (de-commoditize the offering)?*

### **Level 2: De-commoditize**

'Cross-Balance-Sheet' Cross-Sell: After the equity line application is secured, the customer is referred to a financial advisor who illustrates strategies for employing the equity line for the customer to accomplish goals they discuss in their meeting. This is dramatically different than merely providing a check to the customer at the closing.

In the interview, the advisor demonstrates how the customer might pay off their consumer debt, which is not providing a tax savings to customer and is currently at a much higher interest rate. This increased payment savings and the tax benefits from the payoff of the consumer debt could be utilized to save for retirement, and would allow the customer to increase their 401-K contributions at work (adding more tax benefit). Remaining funds are available on the equity line as a cash emergency reserve, thereby releasing funds that the customer had previously set aside in a checking account as an emergency reserve. Those funds could then be invested in a mutual fund account towards the customer's goal of buying a beach house when they retire at age 65. The advisor illustrates this strategy with charts and illustrations that substantiate the financial impact to the customer. The customer realizes 'highly visible' value from what was initially a simple equity line transaction –rapidly moving the customer to Level 2 in the relationship.

### **Level 3: Improved Customer Retention**

The complexity of the relationship now makes the product more difficult to find in a comparable open market environment, moving us through Level 3 by increasing the retention probability of a customer who is experiencing an enhanced outcome due to the value-added process initiated by the lender and the advisor. The customer is invested now in an outcome rather than a stand-alone product, and the likelihood of moving a complex transaction like this to another competitor is more difficult. The ABA has noted that, "When the mortgage is closed...your new mortgage customer has built a relationship with your mortgage loan officer and trusts him as a representative of your bank. Training your mortgage officers about your deposit accounts allows them to sell products appropriate to the customer's life stage."<sup>8</sup>

### **Level 4: Institutions as a Financial Partner**

This solution-based approach moves the providing institution from a 'vendor' who sells products (an equity line) to a 'partner' that provides something far more (the outcome of using an equity line to reduce debt, increase tax savings, fund retirement, and create savings plan for future second home), thereby moving the customer to Level 4 in the relationship.

The increased benefit from the integrated solution provided by an institution who cross-sells across the balance sheet, as opposed to an institution who sells an intra-silo credit product, also reinforces the very value that the financial institution knew was there initially, but had struggled to create due to the inability to stimulate this 'cross-balance-sheet' relationship with a partnership of their internal divisional silos. Within this approach to cross-selling lies the key value proposition for customers and their respective financial service institutions willing to invest in taking their cross-selling to this next level. The benefits to the institution include:

- *Increased income from the sale of multiple new products.*
- *Increase likelihood that customer will remain with institution long term.*
- *Increased likelihood that customer will tell others about their experience, leading to additional referrals.*
- *Increased likelihood that additional new products will be purchased in the future.*
- *Increased likelihood that the loan officer will utilize the financial advisor in the future to partner in customer transactions.*
- *Increased likelihood that the financial advisor will look for future cross-selling opportunities that they can refer to the loan officer.*

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<sup>8</sup> "Cross-Selling to Your Mortgage Customers", Bank Marketing, January/February 2001

While most financial services companies seek to achieve this level of cross-selling success, many are still measuring their success by the number of products they cross-sell to the customer, frequently referred to as the cross-sell ratio.<sup>9</sup> Does this measurement fully assess the institutions cross-selling effectiveness?

### ***Improving Cross-Selling Competencies***

As an institution's cross-sell ratio of products per customer grows, it becomes increasingly more difficult to maintain the rate of growth. For example, a checking account customer might be easily convinced to obtain a credit card or buy a CD at the same bank, but once this "low hanging fruit" has been plucked, additional sales become more challenging. Furthermore, it may be easy to compensate a mortgage loan officer to sell a home equity line of credit to a customer refinancing their home mortgage, but it's an entirely different issue to motivate and train a financial advisor to effectively sell a mortgage solution to his investment clients.

Since our focus here has addressed the capital and credit market convergence, we'll further refine our focus to study the issues related to stimulating a financial advisor (capital market team) to refer or cross-sell to a loan officer (credit market team). We'll base this work on both our own research and the practical experiences of KendallTodd, Inc., a company that has been focusing on this particular area since 1991. KendallTodd has worked to identify barriers and obstacles that must be overcome for these divisional silos at both an institutional and a grass roots level to eliminate these obstacles and establish a 'common dialogue' through which they can refer their respective customers.

### ***The challenge for institutions***

When Wachovia announced their planned merger of Wachovia Securities with Prudential Securities in February 2003, some industry experts questioned the acquisition because, "Prudential brokers are known for being independent-minded, and they might object to Wachovia's efforts to cross-sell bank products."<sup>10</sup> Prudential's advisors are not unique in this respect. Below, we have outlined eight reasons why a typical financial advisor will be reluctant to refer their customer to a loan officer providing mortgage services, and how the financial institution can work to help them view the concerns differently:

- 1) **Challenge:** Financial advisors are worried that a credit decision they have no control over will impact their relationship with their customer. This perceived risk is not worth the perceived return. According to the ABA's *Bank Marketing*, "[brokers] are fearful of putting at-risk their advisory stature with clients for the sake of proprietary product-pushing."<sup>11</sup>

**Actions:** The institution must help the advisor:

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<sup>9</sup> "And they said it couldn't be done", ABA Banking Journal, April 2000

<sup>10</sup> "Wachovia brokerage to merge", Raleigh News and Observer, February 20, 2003

<sup>11</sup> "Is the Cross-Selling Real After a Bank-Brokerage Merger?" ABA Bank Marketing, October 2001



- Perceive the risk to the financial advisor differently.
  - Alter their view on the potential return to the financial advisor.
- 2) **Challenge:** Financial Advisors don't feel the compensation for a mortgage referral is enough to justify the risk or the work involved, and would rather refer the customer to a mortgage lender capable of referring customers to them in the future.
- Actions:** The institution must help the advisor:
- View their compensation in terms of the long term relationship, not solely the immediate transaction value.
  - Illustrate how the immediate compensation value might be meaningful if they learn how to incorporate other product sales to this transaction through the implementation of an integrated cross-balance-sheet sales approach.
  - Consider the risk of giving a customer's financial information to another institution that may/will cross sell other services.
  - Consider the value of subsequent customer referrals that will follow from a successful mortgage closing for their customer.
  - Consider the potential additional sales that will be uncovered through the relationship building that comes with helping the customer with credit based needs to fulfill capital based needs.
- 3) **Challenge:** Advisors are accustomed to assessing a week's productivity by reviewing the following Monday's commission report. "Brokers are used to being paid in the same month they present a product to their client."<sup>12</sup>
- Actions:** The institution must help the advisor:
- Think longer-term.
  - Understand that consistent cross-selling will create a pipeline of referrals that can lead to bigger commissions, new customer nests, etc. This creates an annuitization of commission revenues.
- 4) **Challenge:** Advisors don't feel that it's their responsibility to advise their customers about a mortgage.
- Actions:** The institution must help the advisor:
- Understand that customer satisfaction and loyalty are grounded in how well the advisor is meeting all their financial needs.
  - Realize that a customer relationship on investment performance is a roller-coaster proposition tied to the market. When the market goes down, so do rates, providing an opportunity for the advisor to provide significant value to the customer.
  - Understand that providing advice on non-investment products helps diversify the relationship and de-commoditizes the services being offered, differentiating the advisor from investment-only service providers and further increasing chances of customer retention.

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<sup>12</sup> "Is the Cross-Selling Real After a Bank-Brokerage Merger?" ABA Bank Marketing, October 2001

- 5) **Challenge:** The advisor may not have integrated a comprehensive range of products into his customer communication.

**Actions:** The institution must:

- Help the advisor develop a way to communicate the value of the new products the advisor can offer.
- Provide approved marketing and education tools the advisor can use to increase their confidence.

- 6) **Challenge:** The advisor may not possess the product knowledge to effectively present mortgage solutions.

**Actions:** “Firms have recognized that in order to keep and grow assets they must invest more money in the financial consultant who will need better technology to do the advisory work well.”<sup>13</sup> The institution must help the advisor:

- Understand the similarities and differences between the capital and credit markets.
- Incorporate mortgage lending needs into the overall financial needs of the customer.
- Set basic expectations on how the advisor will be involved in the lending process as an advisor as opposed to a lender.

- 7) **Challenge:** Advisors find it difficult to discuss loan products that often are packaged to their customer with rates and fees that fluctuate differently than their typical product sales.

**Actions:** The institution must help the advisor by:

- Providing an adequate tool to effectively illustrate the factors that the customer might consider related to rates and fees, or provide a simple ‘best deal’ guarantee.
- Providing tools to help the advisor profile customer needs and present unique solutions without necessitating a great deal of training or using industry-specific jargon.

- 8) **Challenge:** Advisors typically avoid the lending business because they’re afraid of having to dedicate a large amount of time to the sales, application and approval processes involved with a mortgage or other loan. In the words of James Gorman, Chairman of Merrill Lynch Private Client Group, the, “DNA of the industry has been sales, and service has been an afterthought.”<sup>14</sup>

**Actions:** The institution must help the advisor:

- Understand their role as a referral source to an internal third party.
- Stay focused in their capacity as a *financial advisor* and not simply an *investment advisor*.

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<sup>13</sup> “The future of the Industry”, Registered Rep., January 1, 2003

<sup>14</sup> “The Future of the Industry”, Registered Rep., January 1, 2003

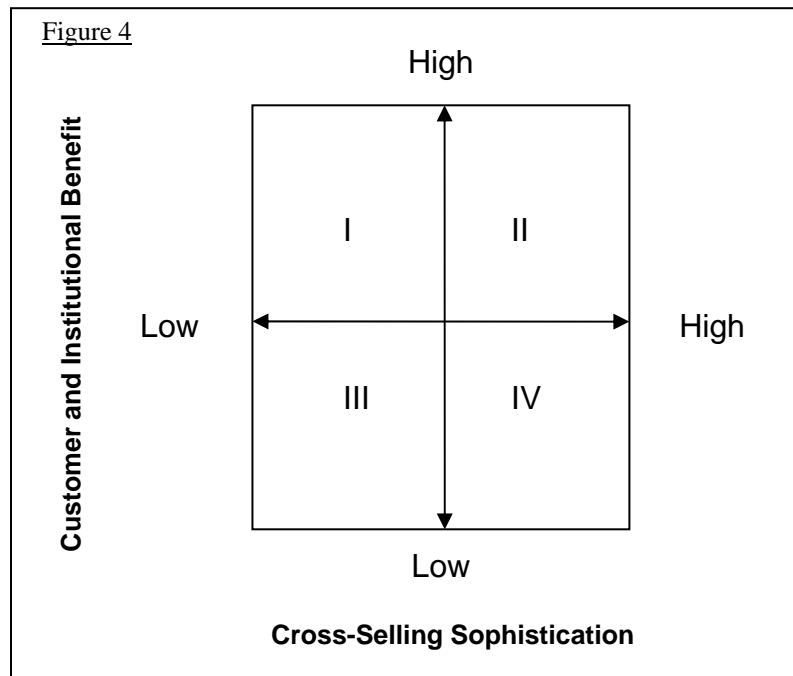
9) **Challenge:** Advisors who have a bad lending experience will be reluctant to pursue cross-selling efforts for an extended period of time.

**Actions:** The institution must help the advisor:

- Recover from a bad lending experience through education, communication, and motivational resuscitation.
- Define the lengths it is willing to go to make this a positive experience for them and their customers.
- Believe that they understand the importance of those customer relationships and are willing to stand behind advisors when they embark on this process.

### ***A Future of Collaboration?***

At the outset of this paper, we discussed how the financial services industry has been investing in a future based on the effective collaboration of their internal divisions, and their external partnerships. What will be the outcome of this scenario? Figure 4 shows four possible outcomes based on 1) the sophistication of an individual institution's cross-selling initiatives, and 2) the individual provider and customer benefit that is ultimately gained from these initiatives. The outcomes are designed to reflect the experience of a specific institution rather than the industry as a whole. Below, we have discussed a description of these four outcomes for the industry and the implications for the institution and customer in each.



**Outcome I – Low cross-selling sophistication, high customer and institutional benefit**

Outcome I represents a scenario where institutions fail to develop a more advanced cross-selling strategy but select individuals within the organization do, increasing customer benefit. Under this outcome, a small percentage of customers would become increasingly loyal and more profitable despite the fact that institutions are not offering fully integrated cross-selling solutions. This scenario is likely to be achieved by only a small group of experienced employees in isolated areas within the institution that create their own systems and procedures to accomplish this outcome. The majority of clients stay in the Level 1 area of our “four levels of cross-selling”, with a few isolated customers moving to Level 4 through their interaction with specific agents of the institution.

**Outcome II – High cross-selling sophistication, high customer and provider benefit**

Outcome II could be considered the ultimate institutional goal, where cross-selling is occurring culturally within the organization and everyone from upper management to line personnel see the integration as part of their service to the customer. Systems, tools, and training continue to provide a foundation that reinforces the development of products and experiences between all divisional silos within the organization. In this outcome an increasing number of customers move from Level 1 to Level 4.

**Outcome III – Low cross-selling sophistication, low customer and provider benefit**

Outcome III may be the default starting point for most institutions due to either the limited time that cross-selling has been a priority or the limited resources the institution has made available for this endeavor. In this scenario, institutions either do not attempt to improve cross-selling strategies, are unable to create a viable cross-sell strategy, or find themselves unable to successfully implement a cross-selling strategy once it has been developed. Over time, competitive pressures will make cross-selling improvements a strategic imperative for institutions. As we have described, there are numerous opportunities to improve cross-selling sophistication at many levels, so at minimum institutions should be able to achieve marginal improvements in their cross-selling strategy over time through mimicking other institutions that are having success in their strategies. Therefore, we do not view outcome III to be feasible in the long run as institutions will be compelled to increase their investment in cross-selling initiatives over time due to competitive pressures. Institutions who fail to invest in their cross-selling strategy will ultimately lose substantial market share to those who do.

**Outcome IV – High cross-selling sophistication, low customer and provider benefit**

Outcome IV might result from an institution investing heavily in technology, but not in training for employees who must bridge the products and services. Substantial improvements to their cross-selling strategies are made, but customers do not see and feel the visible benefit from these strategies and in their eyes the products and services remain commodities. The machine works, but it has no soul. The institution would see improved profitability, but would be unlikely to retain customer at the same level as a competitor. In this outcome, institutional profitability would suffer as institutions fail to gain advantages through their investments. While some institutions may one day find themselves in this predicament, the shortcomings of current cross-selling efforts necessitate that greater benefits will surely be realized by many of them as sophistication increases.

### ***The Final Outcome***

We would hope this paper highlights the urgency with which institutions must invest their attention and resources towards the implementation of a clear cross-selling strategy to meet their customer's financial needs. As a result, the institution should clearly see a payoff through increased wallet share, a de-commoditization of their product offerings, increased customer loyalty leading to greater client retention, and an evolution of the customers' perception of the institution from that of vendor to that of financial partner. Ultimately, the institutions who fail to pursue more sophisticated cross-selling strategies may find themselves in a weak competitive position long-term.

We would suggest that Outcome II is the most likely result for most institutions seek to develop the maximum return on their cross-selling strategy. The ultimate payoff may stem from the fact that those who achieve Outcome II will find themselves in an elite group of institutions that command rich product and service sets that meet their customers' needs in such a way that few customers would risk migration to a competitor. This customer stability and frequency of income producing transactions could establish for the institution a typical customer that is *less* expensive to acquire, *much* easier to keep, and a great deal *more* profitable when they stay.

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**Resources**

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