February 1994 Senior Financial Officer Survey[1]

Summary

Banks continue to expand the provision to their customers of alternatives to deposits, such as mutual funds and other products available through retail brokers.[2] To obtain additional information about bank involvement in this area—and the related area of providing investment advice to mutual funds—the System conducted a Senior Financial Officer Survey of fifty-five large commercial banks.[3] The survey requested information about the availability and profitability of providing brokerage services to retail customers (with emphasis on mutual funds) and the provision of non-brokerage services to mutual funds (primarily investment advisory services). The survey followed up on a Senior Financial Officer Survey conducted last year on bank offerings of mutual funds to retail customers.[4]

This year's survey found evidence that large banks are continuing to expand their retail brokerage programs. The median increase in revenues from retail brokerage activities was 30 percent in 1993. Banks have made their brokerage services more accessible by hiring more brokers and by stationing those brokers at additional branches. In particular, most banks characterized their efforts to sell mutual funds to retail customers as more vigorous than a year ago.

Despite this growth, retail brokerage remains a sideline for most of the banks. More than half of them have fewer than 100 full time brokers, and only a few derive more than a minimal fraction of their noninterest income from such activities or have sold mutual funds to a sizable percentage of their depositors. In addition, many banks have not linked brokered investments to existing bank products and services. For example, only about two-fifths of the banks offer cash

---

[1] Prepared by the Division of Monetary Affairs (Brian Reid, with research assistance by Pamela Vagi).
[2] In this summary, the term *bank* refers to the consolidated bank holding company, including its bank and nonbank subsidiaries.
[3] These banks were drawn from every Federal Reserve District and are generally among the largest in each District. Together, the institutions sampled account for 55 percent of all bank assets, and based on data gathered by Lipper Analytical Services and published in the February 9, 1994 issue of the *American Banker*, the mutual funds advised by these banks account for 77 percent of the bank-advised funds. Conclusions from this survey can be used to characterize the activities of large banks but not the overall banking industry.
[4] Senior Financial Officer Survey on Retail Mutual Funds, Division of Monetary Affairs, Board of Governors of the Federal Reserve System, May 1993.

management accounts, where transfers are made between securities or mutual funds and transaction accounts. Just a few banks permit mutual fund shares to be purchased or sold through an ATM.

Providing non-brokerage services to mutual funds is also a minor but growing bank activity. The median increase in revenues from providing non-brokerage services to mutual funds was 24 percent in 1993, and bank sales of proprietary (bank-advised) funds grew last year. However, the median share of noninterest income derive from these services was under 1 percent.

Retail Brokerage[5]

All but four of the sample banks provide brokerage services to retail customers (question 4), and two of those not offering such services plans to do so within the next two years. Mutual funds are available through all banks with retail brokers (question 7).

Inflows to mutual funds sold by banks continue to come partly from retail deposits. Approximately two-thirds of the institutions that were moderately or very confident that they could measure the share of mutual fund inflows coming from retail deposits at their banks estimated that between one-third and two-thirds of their mutual fund sales came from this source (question 15). Less than 15 percent estimated that two-thirds or more of the mutual fund sales came from deposits. These shares are comparable to those reported on last year's survey.

In addition to mutual funds, most institutions also sell annuities, stocks, bonds, and options to retail customers (question 7). Other financial investments available from bank retail brokers include futures contracts, unit investment trusts, and precious metals. In conjunction with their retail brokerage programs, about one-quarter of the banks offer "wrap accounts" (question 12), which are retail brokerage packages providing investment advice and portfolio management services for a flat fee. Somewhat under one-half of the institutions anticipate offering this service in the next two years.

---

[5] Some of the banks were unable to answer all of the questions on the survey. The reported percentages are for those institutions answering the questions. The tabulated results indicate the number of institutions answering each question.

While nondeposit investments are widely available at these large banks, most banks do not combine them in a package with deposit products. Only about two-fifths of the banks offer cash management accounts (question 11), which are packages of money management products that often include a transaction account, credit or debit card, money market mutual fund, and an automated sweep arrangement. Additionally, banks can facilitate transfers between mutual funds and deposits by permitting customers to buy and sell mutual fund shares through ATMs. Here again, only a few banks permit such transactions (question 13). Although combinations of nondeposit investments with deposits are not yet widely available, half the banks plan to offer cash management accounts in the next two years, and 36 percent intend to permit customers to conduct mutual-fund share transactions through ATMs.

Banks are intensifying efforts to market their brokerage services to retail customers. More than 70 percent of the institutions characterized their efforts to sell mutual funds as more vigorous than last year; none reported being less vigorous (question 16). These findings are similar to those of last year, when 90 percent of the banks reported that their efforts to market stock and bond mutual funds were more aggressive in 1993 than in 1992. While banks still have not attracted a large proportion of their depositors as brokerage clients, their customer base has expanded. Sixty-one percent of the banks reported that between 1 and 5 percent of their retail depositors had purchased mutual fund shares through the bank's brokers (question 14). This share is up from 1990, when most banks had sold mutual funds to less than 1 percent of their retail depositors.

The number of retail brokers at banks remains small, though it has grown in the past few years. Only ten institutions have more than 200 dedicated (full-time) brokers (question 9a), but this is up from three years ago when just one bank had a sales force of that size (question 10a). Growth is evident as well in the median number of dedicated brokers, which increased from less than 50 three years ago to between 50 and 100 currently. As banks have entered the retail brokerage business and increased the size of their retail brokerage staffs, a smaller share of their investment sales representatives hold a Series 7 license than did three years ago (questions 9c and 10c), possibly reflecting the recent bank emphasis on selling mutual funds rather than providing a broad range of brokerage services.[6]

Although many banks started with a small number of brokers a few years ago, most of the institutions did not build their sales forces with NASD-licensed dual employees--individuals who sell securities and insurance products and also perform other duties for the bank. Most banks continue to have fewer than fifty dual employees (questions 9b and 10b). Instead, banks tend to assign brokers to several branches. Three-fifths of the banks have sales personnel available on a daily basis at less than 20 percent of their branches (question 8), but more than half of the banks provide brokers on a regular basis or by appointment at over 80 percent of their branches. These coverage ratios are up somewhat from last year and are much higher than in 1990.

This year's survey requested revenue and cost data associated with retail brokerage activities for 1992 and 1993 (questions 5 and 6). For banks able to provide data for both years, the median increase in revenues was 26 percent in 1993 (not shown), and the median increase in net income (gross revenues less gross expenses) was 18 percent (not shown). Still, the impact on overall bank revenues and net incomes from such services remains small. In 1993, the median revenue was $6.0 million, up from $4.6 million in 1992. A quarter of the respondents had revenues above $17.2 million and a quarter had revenues below $3.2 million in 1993, suggesting widely varying levels of involvement in retail brokerage services. The median cost of providing these services was $3.1 million in 1992 and $4.1 million in 1993. Half of the banks derived less than 2 percent of their noninterest income from retail brokerage activities in 1993 and only about 1 percent of their pre-tax net incomes (not shown).

Proprietary Mutual Funds

Proprietary mutual funds are advised by banks and are typically brokered exclusively through sales staff associated with the advising bank. Forty-eight of the sampled banks provide investment advice to mutual funds, and four of those not advising funds plan to do so in the next

---

[6] A sales representative with a Series 6 NASD license is permitted to sell packaged investment products such as mutual funds. A Series 7 license permits a broker to sell packaged investment products and non-packaged investments such as stocks and bonds.

two years. The median gross revenue from providing these non-brokerage services to mutual funds was $6.5 million and $5.4 million in 1992 and 1993, respectively (question 2). For institutions able to report revenue data in both years, the median increase was 24 percent (not shown).[7]

The extent to which banks provide non-brokerage services to mutual funds varies widely among the sample banks. A quarter of the respondents earned less than $2.1 million in 1993, but a quarter earned more than $17 million. For the banks that could report cost data (question 3), the median cost of providing these services was $2.9 million last year, with half of the banks reporting expenses between $0.8 million and $8.4 million. The median net income as $3.1 million last year, up from $2.4 million in 1992 (not shown). Banks in the lower quartile had net incomes under $0.6 million, while banks in the upper quartile had net incomes above $6 million.

Most banks obtain only a small fraction of their noninterest income from these activities. In both 1992 and 1993, the median share of noninterest income derived from providing non-brokerage services to mutual funds was less than 1 percent (not shown). Net incomes for these activities were tiny as well, contributing less than I percent to the net incomes of half of the banks.

Bank sales of proprietary bond and stock funds grew more rapidly than sales of nonproprietary funds (question 17).[8] The median dollar volume of proprietary bond and stock fund sales was $50 million in 1992 and $135 million in 1993. For banks able to report proprietary stock and bond fund sales data in both 1992 and 1993, the median increase was $32 million and the median percentage increase was 114 percent. In comparison, the median dollar volume of nonproprietary bond and stock fund sales was $67 million in 1992 and $84 million in 1993. For institutions able to report in both years, the median dollar volume rose $31 million, and the average percentage increase was 56 percent.

Some banks have seeded their proprietary mutual funds by transferring discretionary funds, such as collective investment funds, from their trust departments into bank-advised mutual

[7] The decline in median revenue between 1992 and 1993 was because the additional banks reporting in 1993 generally had lower revenues than the banks that reported in both years.

[8] Respondents were asked to report gross redemptions and sales of proprietary and nonproprietary stock, bond, and money market mutual funds. Most banks were unable to provide the gross sales for money market funds and gross redemptions for any of the funds; therefore, the responses to these questions have been excluded from this summary of the survey results.

funds. Such transfers of funds do not increase the volume of assets under bank advisement. However, most institutions reported that such transfers accounted for a small share of their proprietary mutual fund sales. Half of the institutions attributed less than 20 percent of their 1992 proprietary fund sales to conversions (question 18). In 1993, such conversions accounted for less than 20 percent of the sales at nearly three-fifths of the banks (question 19).

To better understand the developments in markets for non-deposit investment products, the Federal Reserve System is seeking information from bank holding companies concerning their activities in the mutual fund industry.

The term "bank holding company" refers to the consolidated entity, including bank and nonbank subsidiaries.

Italicized words and phrases are defined in the glossary located on the final page.

1. Does your bank holding company offer *proprietary* mutual funds?

Number of Banks (Percent)

a. Yes	b. No, but expect to offer *proprietary* funds in the next two years	c. No, and do not expect to offer *proprietary* funds in the next two years	Total Banks
48 (87.3)	4 (7.3)	3 (5.5)	55

2. What were your bank holding company's gross revenues from providing services **other than brokerage services** to mutual funds (e.g. administrative, investment advisory, etc.) in 1992 and 1993?

Year	Banks	75th Percentile ($ millions)	Median ($ millions)	25th Percentile ($ millions)
1992	39	11.431	6.500	1.094
1993	46	17.000	5.357	2.113

3. What were your bank holding company's costs from providing services **other than brokerage services** to mutual funds (e.g. administrative, investment advisory, etc.) in 1992 and 1993?

Year	Banks	75th Percentile ($ millions)	Median ($ millions)	25th Percentile ($ millions)
1992	34	7.300	2.996	0.900
1993	40	8.350	2.981	0.850

4. Apart from trust services, does your holding company provide brokerage services to retail customers either through a *third-party firm* or an in-house brokerage firm?

Number of Banks (Percent)

a. Yes	b. No, but expect to offer these services in the next two years	c. No, and do not expect to offer these services in the next two years	Total Banks
51 (92.7)	2 (3.6)	2 (3.6)	55

If your bank holding company does not offer retail brokerage services, go to question 17.

5. What were your bank holding company's gross revenues from providing brokerage services to *retail customers* in 1992 and 1993?

Year	Banks	75th Percentile ($ millions)	Median ($ millions)	25th Percentile ($ millions)
1992	46	12.800	4.624	2.400
1993	48	17.200	6.050	3.231

6. What were your bank holding company's costs from providing brokerage services to *retail customers* in 1992 and 1993?

Year	Banks	75th Percentile ($ millions)	Median ($ millions)	25th Percentile ($ millions)
1992	45	8.600	3.100	1.600
1993	45	12.000	4.111	1.900

7. What products are available through your bank holding company's retail brokers (including staff provided by *third-party firms*)?

Product	Banks	Percent
Mutual Funds	51	100.0
Annuities	45	88.2
Stocks	47	92.2
Bonds	48	94.1
Options Contracts	38	74.5
Futures Contracts	5	9.8
Other	15	29.4
Total	51	

8. a. Approximately what share of your bank holding company's banks' branches have *dedicated or dual employees* with at least a *Series 6 license* available to *retail customers* on a daily basis (including staff provided by *third-party firms*)?

Share	Banks	Percent
None	10	20.8
<5%	6	12.5
5 to 10%	4	8.3
11 to 20%	9	18.8
21 to 40%	8	16.7
41 to 60%	2	4.2
61 to 80%	3	6.3
81 to 100%	6	12.5
Total	48	

b. Approximately what share of your bank holding company's banks' branches have *dedicated or dual employees* with at least a *Series 6 license* available to *retail customers* on a regular basis (or by appointment) but not on a daily basis (including staff provided by *third-party firms*)?

Share	Banks	Percent
0 to 20%	10	20.8
21 to 40%	6	12.5
41 to 60%	2	4.2
61 to 80%	4	8.3
81 to 90%	3	6.3
91 to 95%	2	4.2
Over 95%	21	43.8
Total	48	

9. a. Approximately how many *dedicated* employees with at least a *Series 6* license does your bank holding company have (including staff provided by *third-party firms)?*

Number	Banks	Percent
Under 50	22	43.1
50 to 100	9	17.6
100 to 200	10	19.6
200 to 300	4	7.8
Over 300.	6	11.8
Total	51	

b. Approximately how many *dual employees* with at least a *Series 6 license* does your bank holding company have (including staff provided by *third-party firms*)?

Number	Banks	Percent
Under 50	41	80.4
50 to 100	3	5.9
100 to 200	3	5.9
200 to 300	0	0.0
Over 300	4	7.8
Total	51	

c. Approximately what share of your bank holding company's sales representatives have at least a *Series* 7 *license* (including staff provided by *third-party firms)?*

Share	Banks	Percent
0 to 20%	5	10.0
21 to 40%	11	22.0
41 to 60%	9	18.0
61 to 80%	6	12.0
81 to 100%	19	38.0
Total	50	

10. a. Approximately how many *dedicated employees* with at least a *Series 6 license* did your bank holding company have three years ago (including staff provided by *third-party firms)?*

Number	Banks	Percent
Under 50	30	58.8
50 to 100	6	11.8
100 to 200	5	9.8
200 to 300	1	2.0
Over 300	0	0.0
None	9	17.6
Total	51	

b. Approximately how many *dual employees* with at least a *Series 6 license* did your bank holding company have three years ago (including staff provided by *third-party firms)?*

Number	Banks	Percent
Under *50*	35	68.6
50 to 100	2	3.9
100 to 200	1	2.0
200 to 300	0	0.0
Over 300	0	0.0
None	13	25.5
Total	51	

c. Approximately what share of your bank holding company's sales representatives had at least a *Series* 7 *license* three years ago (including staff provided by *third-party firms)?*

Share	Banks	Percent
0 to 20	8	15.7
21 to 40	2	3.9
41 to 60	4	7.8
61 to 80	4	7.8
81 to 100	24	47.1
None	9	17.6
Total	51	

11. Does your bank holding company offer retail *cash-management accounts* that link traditional bank deposits with nontraditional bank products?

Number of Banks (Percent)

a. Yes	b. No, but expect to offer this product in the next two years	c. No, and do not expect to offer this product in the next two years	Total Banks
19 (37.3)	25 (49.0)	7 (13.7)	51

12. Does your bank holding company offer *wrap accounts* to *retail customers*?

Number of Banks (Percent)

a. Yes	b. No, but expect to offer this product in the next two years	c. No, and do not expect to offer this product in the next two years	Total Banks
11 (22.0)	23 (46.0)	16 (32.0)	50

13. a. Can your bank holding company's *retail customers* transmit and receive funds in connection with customer orders to make additional purchases and to redeem shares of mutual funds through your bank holding company's ATMs?

Number of Banks (Percent)

a. Yes, but only for money market mutual funds	b. Yes, for money market and stock and bond mutual funds	c. No, but expect to offer this service in the next two years	d. No, and do not expect to offer this service in the next two years	Total Banks
3 (6.0)	1 (2.0)	18 (36.0)	28 (56.0)	50

b. Is there a transaction fee associated with using an ATM to transmit and receive funds in connection with customer orders to purchase and redeem shares of mutual funds (do not include any penalty fees such as a back-end load)?

Number of Banks (Percent)

Yes	No	Total Banks
1 (25.0)	3 (75.0)	4

c. When are funds from redeemed shares available if the transaction is conducted on an ATM?

Number of Banks (Percent)

Same Business Day	Next Business Day	Other	Total Banks
3 (75.0)	1 (25.0)	0 (0.0)	4

14. Approximately what share of your retail depositors own mutual fund shares acquired through brokers or other sales representatives available through your bank holding company (including staff provided by *third-party firms)?*

Share	Banks	Percent
Under I%	11	22.4
1 to 5%	30	61.2
6 to 10%	6	12.2
11 to 15%	0	0.0
16 to 20%	0	0.0
Over 20%	2	4.1
Total	49	

15. a. How confident are you that you can measure the percentage of the inflows to mutual funds at your bank holding company that were from retail deposits held with your bank holding company's bank subsidiaries in 1993?

Number of Banks (Percent)

Very Confident	Moderately Confident	Unsure	Total Banks
10 (20.0)	24 (48.0)	16 (32.0)	50

If you answered with option c, go to question 16.

b. Approximately what percentage of the inflows to the mutual funds through your bank holding company do you estimate came from retail deposits held with your bank holding company's bank subsidiaries in 1993?

Number of Banks (Percent)

Over 2/3	Between 1/3 and 2/3	Less than 1/3	Total Banks
5 (14.3)	23 (65.7)	7 (20)	35

16. How would you characterize your bank holding company's efforts to sell mutual funds to *retail customers* compared with a year ago?

Number of Banks (Percent)

Much more vigorous	Somewhat more vigorous	About the same	Somewhat less vigorous	Much less vigorous	Total Banks
18 (36.7)	17 (34.7)	14 (28.6)	0 (0.0)	0 (0.0)	49

17. What were the dollar volumes of sales of stock and bond mutual funds conducted through your bank holding company, including *third-party firms* associated with your bank holding company, in 1992 and 1993?

1992

Product	Banks	75th Percentile ($ millions)	Median ($ millions)	25th Percentile ($ millions)
Proprietary and *Private-Label* Stock and Bond Mutual Funds	27	200.000	50.000	10.700
Non-proprietary Stock and Bond Mutual Funds	32	153.884	66.997	26.450

1993

Product	Banks	75th Percentile ($ millions)	Median (S millions)	25th Percentile ($ millions)
Proprietary and *Private-Label* Stock and Bond Mutual Funds	37	500.000	135.000	16.200
Non-proprietary Stock and Bond Mutual Funds	36	215.970	84.500	40.500

18. What share of your sales of *proprietary* and *private-label* mutual funds were conversions of discretionary accounts over which some unit within your bank holding company exercised investment discretion (e.g. collective investment funds, non-collective investment funds, employee benefit trusts, etc.) in 1992?

Share	Banks	Percent
0 to 20%	27	52.9
21 to 40%	4	7.8
41 to 60%	2	3.9
61 to 80%	3	5.9
81 to 100%	4	7.8
N/A	11	21.6
Total	51	

19. What share of your sales of *proprietary* and *private-label* mutual funds were conversions of discretionary accounts over which some unit within your bank holding company exercised investment discretion (e.g. collective investment funds, non-collective investment funds, employee benefit trusts, etc.) in 1993?

Share	Banks	Percent
0 to 20%	30	58.8
21 to 40%	1	2.0
41 to 60%	7	13.7
61 to 80%	2	3.9
81 to 100%	4	7.8
N/A	7	13.7
Total	51	

Glossary

Cash-management account - A product line offering a package of products that may include a transaction account, a savings account, a credit/ debit card, a brokerage or mutual fund account, or an automated sweep arrangement

Dedicated employee - An employee whose sole responsibility is to sell securities and insurance products

Dual employee - An employee who sells securities and insurance products and also performs other duties for a bank subsidiary

Non-proprietary mutual funds - Mutual funds other than proprietary or private-label funds

Proprietary mutual funds - Funds advised by the bank holding company

Private-label mutual funds - Funds sold exclusively through the bank holding company but not advised by it

Retail customer - A client other than a corporation, business, or trust account

Series 6 license - An NASD license permitting an individual to sell packaged investment products such as mutual funds and annuities

Series 7 license - An NASD license permitting an individual to sell packaged investment products as well as non-packaged investments such as stocks and bonds.

Third-party firm - A securities brokerage firm that provides services to financial institutions on a third-party basis

Wrap account - An investment product that charges a flat fee for investment advice and portfolio management services