

Nexity and the us banking industry

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Introduction of Nexity
Nexity is an online bank, which was initially called the People State of Grand and it was opened in February 2000. Its headquarters are located in Birmingham, Alabama, USA.

Currently, David Long is the President of Nexity and Greg Lee the CEO. The turnover represented an amount of \$13, 018 millions in 2003. Banking online is a very good opportunity for the banking industry, there was a projection of 67 million of American using it by 2007 compared to 38 millions by 2003. There were a lot of players in this competitive market but Nexity had a generic strategy of differentiation by spreading its geographic and demographic customer base throughout the US.

External Analysis Industry and Demand Analysis

Historically, there was a rebound of the banking industry and rapid growth in this area after the Great Depression and World War II, with the hope to keep the industry from being highly concentrated. Indeed, the US banking industry was a fragmented and dispersed system but it changed in the 1980's. These changes were due to financial legislation which wanted to lead to a more integrated financial system in US in terms of activities and products. The deregulation led to consolidation and consequently to new rivalry.

Helped by the Gramm Leach Bliley's Act offering extended banking but also by the changes in communication and information technologies, the US

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banking industry knew a merger mania and a lot of acquisitions were done. All had the same goal : to develop a more national brand recognition in a market newly concentrated. But scandals also appeared due to these new changes. Concerning the size of the industry, it is obvious that the concentration could be seen between 1980 and 2002.

Number of institutions declined from 14, 434 to 7, 887 contrary to their branches which raised a lot from 38, 738 to 66, 185. However it is important to make the distinction here between two types of banks. At first, there were the brick-and-mortar banks and then appeared the virtual ones, such as Nexity. Now, let's compare Nexity in the US virtual banking environment by a review of the main actors performances in 2002.

Institution	Assets (in thousands)	Deposits (in thousands)
E*Trade Bank	\$17, 453, 676	\$9, 157, 328
ING Direct	16, 142, 091	13, 112, 826
NetBank	4, 280, 899	2, 479, 421
Principal Bank	1, 967, 342	1, 826, 018
BMW Bank of North America	1, 149, 732	156, 983
National Interbank	645, 448	528, 516
Nexity Bank	501, 167	368, 523
American Bank	472, 181	336, 288

Here we can see that Nexity is the 7th virtual bank on the market in terms of assets. More important, we also notice that E*Trade Bank and ING Direct are the first and second ones, with a huge gap separating them from the others, among which competition is really hard. Porter's five forces

Even though there are less and less institutions since the 1980's, there is still a high rivalry among the competitors in virtual banks. Clients are more and more oriented to the more rentable channels like internet and ATMs. Virtual banks consequently deliver a lot of services but only through internet that allow to reduce costs in occupancy and salaries in order to offer better rates

of interest (to 3 times better than averages). Virtual low-costs positioned banks compete against other virtual banks with good customer service, in-house customer data and service center operations, strong management teams, a good mix of attractively priced products, and low marketing costs.

It's a price competition which includes lower margins directly. What about the entry barriers with potential entrants? It is a low threat. The largest barrier to entry is the expenses in founding a bank: a new bank needs to raise 8-12 million to begin operations. But start-up costs for virtual banks are much less expensive than for traditional banks: virtual banks could begin operations for millions less than traditional banks (no offices, etc.) , even though they'll have to invest a lot in marketing and advertising budgets in order to attract depositors at the start-up time. The second barrier is loyalty to older, larger, and more established brand-name banks.

Here we can talk about a network effect. And third, an existing bank holding company provides investments and backing for the new bank by spinning off a separate banking entity. Concerning the substitutes, the only ones could be traditional banks because people need safety and want to be sure about their money by advice. There would be a switch from virtual banks to brick-and-mortar ones, because people are deceived or want to experiment again the first one, with a better consideration of its advantages. But there is less possibility for this than the opposite because people want more and more to gain time. That's why there is a low threat of substitutes. Clients are the buyers.

They have a relative bargaining power especially on the rate of interest on borrows. The first have an interest to bargain and have a bargaining power

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because of the rate of interest as a complement revenue and because banks need liquidity to operate. He can have some influence on the bank with other clients. Word of mouth works a lot with a service you use daily. Brand recognition also can be negative. Suppliers: They are the companies that provide inputs/services that banks purchase in order to be able to borrow and lend money. It can be a safety certificate for online web, labels...etc. With an environment impacted by scandals, they can have a bargaining power but it is still relative because there are a lot of suppliers. ==> Internal rivalry, Buyers and Suppliers are the strongest forces in the US online bank industry, whereas potential entrances and substitutes are the weakest.

Key Success Factors can consequently be defined for this industry: forecasting all the marketing and communication budget for implementing and then keeping talking about the bank for new customers; using the more rentable channels for the customers; offering low rate of interest in borrowing and high for revenues to client and convincing people of the value of virtual banks ; implementing more and more safety with technologies.

PEST Analysis One of the main points in the external analysis is the PEST analysis. The goal of this part is to determine which are the main external forces affecting the US banking industry.

Then, we will introduce and analyse in the following development which factors impact directly positively or negatively this sector in dividing them on the political, economic, social and technological views. On the political view, the US government has a place of protagonist in the current US banking system. In fact, US government launched series of laws which have completely changed the US banking landscape such as the Reigle-Neal

Interstate Banking and Branching Efficiency Act and the Gramm-Leach-Bliley Act. The first one allowed a bank holding company to buy another bank anywhere through the United States without taking into account the state law. The second one allowed affiliation between banks, securities firms and insurance company.

Logically, this deregulation, or the opening of state market that it includes, has strongly impacted the US landscape in increasing the competition on the national area. Moreover, the deregulation led to a merger mania that is to say institutions use a process mergers and acquisitions in integrating vertically and/or horizontally in order to have more costumers and so to gain market shares, and to develop the range of products and services. Finally, the impact of the US government could be seen as an opportunity for banks (the biggest currently) which got out as leaders to the deregulation and merger mania because the market is bigger but as a threat for banks which went to bankrupt.

It's significant to notice how the Fed affects the economy and the US banking system through the actions on the real interest rates. In fact, because the Fed can set the nominal funds rate as a sole supplier of reserves for US banks. But it can influence too the real interest rate thanks to the set of the monetary policy that will operate in the future (the monetary policy of tomorrow influences the real interest rate of today). Then, the Fed has a direct impact on the level of the real rates and consequently on the whole of economy. For example, if the real rates are lower, the activity of banks will increase because borrowing costs will decrease and investments from households will increase in order to buy goods or services.

Increasing of consumption from householders will boost the different industries which will invest in capital, in production capacity or in labour (decrease of unemployment). Reducing real rates will get investments as common stock more attractive and will boost the US internal business in limiting imports because the foreign exchange value of the dollar is reduced and so, the foreign product get more expensive. On the economic point of view, multiple factors should be taken into account. One of the most significant points is the interest rate which is developed upside. Finally, that represents an opportunity if the real rates are declining and rather a threat if it is growing. Moreover, other non-negligible point is the purchasing power of households.

In fact, according to some economic theories, an increasing part of households' consumption is oriented to service expenses on the one hand, and, on the other hand, other certain part of it matches to savings. Generally speaking, a growing purchasing power represents an opportunity for banks because deposits increase and the banks are more resources for investments on financial markets. But it's essential to notice that two significant elements have a direct impact on the purchasing power of households: the unemployment rate and the inflation rate. Effectively, if the unemployment rate is increasing and/or if the inflation rate is superior to the increasing rate of wages means that the global purchasing power is decreasing.

Social factors impact directly the US banking system because of the diversity of the population, the demography, the differences of client expectations concerning bank services... all of these elements play a role on the

behaviour of the clients. The first point that we have to take into account is the fact that an average customer wants to have trust and confidence in his financial institution. That's why banks have to reassure their clients about the financial health of the institution, about the quality of the offered services and about the security of the operating system. That is a positive impact for oldest banks which have developed a brand name and focused on a client-loyalty strategy or for biggest institutions which bring proof to the financial health. But through the analysis of the demography, we can categorise the population.

For example, old people prefer to keep a physical contact with the banker in opposition to youngest people which have more confidence and more ability to make financial operations on new channels as internet. Moreover, we can distinguish clients in function of their expectations: long-term engagement combined with quality of services against short-term engagement with profitability (hit-and-run customer for example). This categorisation of the population linked to a particular behaviour can be seen in parallel to the age, race, social level, kind of job occupied... then we can say that it's more an opportunity for traditional banks which offer a largest range of products and channels.

Concerning the technological factors what is significant to put in relief is the technological improvements perceived as an opportunity for banks and the threat of hackers linked to this new technologies. In fact, thanks to the technological improvements, banks have more and more ways to meet the consumers themselves and these needs. Banks use different ways to satisfy clients such as ATMs, debit cards, call centers and telephone banking,

wireless banking and internet sites. These are channels to keep a constant contact with the client for different reasons and to be all the time available to respond to any demand. Moreover, banks develop strategic technology partnerships (like Fiserv for Nexity for example) in order to save the cost of technology and to have the last updated software.

Updating software limits the risk of hacking and restores confidence of clients about the security on the account financial information. But even if a regular updating software and a reinforcement of the security, the threat of hacking stays pervasive. Furthermore, with the development of internet, we have seen emerged a new kind of competitors for the traditional banks which are the virtual banks as Nexity or ING Direct. INTERNAL ANALYSIS Nexity gets the opportunity to growth quite fast and its profitability could be High. In order to understand the most appropriate strategy of the company, we will try to highlight its different aspects by presenting its Resources View Analysis and its Value Chain. A. Resources View Analysis.

As the matrix exhibit 7 shows us, the company benefit of a high improvement of its assets that reinforce its capacity to provide a high level quality range of products

Tangible asset: Due to its activity, the company owns few tangible asset. In fact, its services allow it to only get some offices from its acquisition of People bank of Alabama with 30\$ in asset. The company have also a competitive advantage thanks to the location of its call centre that facilitate the exchange of data between the main office and the call centre.

Intangible asset: By getting a top tier award from Bankrate for its High yield on money market accounts and certificate of deposit, the

company proves to its customers its efficiency and in capacity to provide good quality products.

By acquiring People bank of Alabama, Nexity has get as well a know-how of over 100 years, which gives it a significant advantage compare to its competitors, as it has enjoyed the different expertises made by the former company so it has been able to produce High quality products but also reinforce the formers one adapting them to the new requirement of the market, and it remains also a good point for its advertising with it customers: they can focus it with the over 100 year of experience which people are sensitive with. It also ahs the Web Trust Seal accreditation that is a certification from the services of the American Institute of Certificate Public Accountant and the Canadian Institute of Chartered Accounts. It proves that its website delivers safe services. So it reinforces the trust its customers give it but also can be very useful in order to attract new one and to spread its market.

Capabilities : By getting its break-even point in only 18 month, Nexity has a strong competitive advantage compare to most of its competitors that usually get it in 3 years average. That is to say the company can invest money in R&D for example in order to create and provide highest quality product. It proves that the company realises large economy of scale, that it is highly efficient to get result and it is as well relevant that it is very successful. Its renowned customer service, which has a very good image with its Customer, as it remains friendly and quick, allow the company to keep its customers as they trust it to give them High quality services.

It is the result of the proximity between the main office and the call centre: employees are able to provide High quality answers to customers as they keep being updated about the characteristics of the products and services and the evolution of them. The competitors cannot give as quick answer as Nexity does because they might have their call centre farer away from their office, and maybe abroad, sot hey cannot give more relevant answer as Nexity does. By reimbursing customers using other ATM than Nexity's ones, the company can meet some weaknesses as it costs it quite a lot of money

Value chain analysis Firm infrastructure: The firm has a main office with all the facility costs to support, and its call centre with the same type of costs.

So all those generic costs are not a constraint for Nexity and they can concentrate their budget to the R&D or to the improvement of its strengths such as the customers service. Human resources management: The main cost is due to the call centre as the company is very focused to give a high customer service. Technology development: Nexity website is highly renowned as it gets the Web Trust Seal accreditation, which is a proof of quality for a company that uses the Internet for its distribution channel

Inbound logistics: As the company provides services, it only has to increase if necessary its tangible and intangible assets. So it has not have to deal with any inbound logistic and it is a strength for its economy of scale politic.

Operation:

This might be the main department of the company as employees from the call centre with present the different product but also supply strong customer services; and those to point are the most important one for the firm to provide a competitive advantage compare to its rival. Marketing and

sales Focusing on an Internet-based advertising channel like Bankrate. com, the company invest quite a lot to improve its visibility in order to attract as many people as possible throughout the 50 states of the USA. The fact that Nexity proposes a lot of products and services constraints them to spend a lot because they want to provide the best services. This is the result of adopting a differentiation strategy based on reducing costs. Services:

The company provides a strong customer service in order to keep them as they can be very versatile and find another bank if they are unsatisfied. So it is very important for Nexity to be focused on that and the fact that call centre employees are close to the main office give them a qualitative advantage as people mainly remains satisfied. Nexity Financial analysis A. Nexity bank business model and strategies. Nexity bank is a virtual bank wich works only on internet and earns money from interests rates based on loans. Nexity is build from traditional banking practices, that means this bank is able to deliver all the advantages and financial products[1] as a normal bank but with no branche.

David Long and the others managers decided to applied for their bank the « Blue Ocean Strategy » wich links at the same time « differentiation and low costs strategies ». One can talk about blue ocean strategy, because the market was not established and competitors were not really present in this sector. This strategy aims to create a new market space and to make competition irrelevant. Nexity's builders knew that, if they were able to propose at the same time good quality products with attractive interest rates coupled with an efficient call centre they will earn market shares and money. These criterias permitted to develop the Nexity's strength, and one can

observe that the differentiation is based on these same criterias : an efficient call center and good quality product at the lowest price.

If Nexity has attractive interest rates, is just because, it doesn't have to pay high overhead costs (no branches) so Nexity can pay more interest on deposits and charge lower rates on loans. This is the second part of the « blue ocean strategy », the « low costs » strategy because adopting this concept Nexity attracts price-sensitive consumers. Nexity has the lowest interest rate for the checking but has the highest for One-year Certificate Deposit and Money Market. That means, Nexity wants to keep its consumer. Nexity doesn't want to be a simple bank where consumers only want to check their accounts. Nexity prefers to have people whose need loans and are engaged with the bank. Moreover, Nexity proposes bank's services and bill pay online.

With these offers, the bank aims to work with people between 32 and 49 years old, with an income average of \$81, 600 and investible assets of \$320, 300 and these persons spend at minimum 27 hours per week on the internet. So these people have money and spend many time on the internet that permits to the bank to benefit of « good quality » consumers. Finally one can underline that Nexity adopt also the « low cost strategy » for its advertising. In fact they did all their advertising on the Internet so they benefited of a huge advertising campaign at the lowest price. Nexity Financial Analysis. Previously, one observed the strategies employed by Nexity in order to become an important actor in the US (virtual) banking industry. Now, it's important to know if these strategies are efficient or not.

Firstly, if one look at the bank net income growth, one can observed that the net income had grown by 181% in 3 years, from \$-3, 032, 000 in 2000 to a profit of \$2, 461, 000 in 2003. This is really important growth wich reflects the good health of the business. [pic] Evolution of the net income between 2000 and 2003 One can also observe if the bank respects its strategies. The turnover has grown by 250% in three years wheras the overheads grown by only 16%. So Nexity respects the strategy of keeping overheads costs low in order to offer interesting interest rates. If one looks at the distribution of the turnover between the interest income and noninterest income, it can observe that the Nexity makes 97. 1% of its turnover with interest rates and only 2. 79% with the noninterest rates. Secondly, it is interesting to observe some financial ratios : - The coumpound annual growth wich gives the annual growth rate. And for Nexity, this ratio is around 30%. It is a good indicator for the company's development. - The return on equity, wich is relevant for a bank because it gives the bank's profitability by revealing how much profit the bank generates with the money shareholders have invested. For Nexity, the ROE passed from -32, 71 in 2000 to 12, 99 in 2003. One can easily observed that in three years Nexity learnt how to make money with shareholders investments. The efficiency ratio evaluates the overhead efficiency structure of a Financial institution. Banking is no different from any industry. If the bank wants to survive the bank has to keep overhead costs down.

The efficiency ration permits to measure how the bank is operating, how much money the bank must spend to generate each dollar its bring on. In the Nexity case, this ratio is getting lower and it is good for the bank ans its

shareholder. . In fact the ratio passed from 230. 69 in 2000 to 63. 54 in 2003. Lower the ratio, better it is for the bank. So, one can conclude that Nexity respects its commitments because the bank makes money from interest rates and keeps its overhead costs low. SWOT ANALYSIS STRENGTHS | Large range of product | | High satisfaction of customers | | High quality of customer services | | Many awards from Bankrate(high quality of products | | High efficiency of the website(Web Trust Seal Accreditation | | Strong expertise thanks to the acquisition of People's bank of Alabama (over 100 years of | | experience in the Banking sector) | | Growth of its assets (over + 400% from July 00 to July 2003) | | Good compound annual growth | | WEAKNESSES | Some costs can be avoid (ATM reimbursements) | | Increase of other borrowed funds that has to be controlled | | OPPORTUNITIES | Impact of the American government with the deregulation of the market (advantages for | | leaders | | Internal rivalry buyers and suppliers | | Forecasting all the marketing and communication budget | | Bank and bill pay online customers present the most interesting profiles (high income and | | lots of investable assets) | | THREATS | Hard to attract new customers as they rely a lot on their old financial institutions. | | Hackers | | New competitors should appear | TOWS ANALYSIS | STRENGTHS | WEAKNESSES | |

Large range of product | Some costs can be avoid (ATM | | High satisfaction of customers | reimbursements) | | High quality of customer services | Increase of other borrowed funds that has| | Many awards from Bankrate(high quality of products | to be controlled | | High efficiency of the website(Web Trust Seal Accreditation | | | Strong expertise thanks to the

acquisition of People's bank of Alabama (over 100 years of experience in the Banking sector) Growth of its assets (over + 400% from July 00 to July 2003) Good compound annual growth OPPORTUNITIES | Improve the advertising on internet and traditional media channel in | Open a new office in another state in | Impact of the American government with the deregulation | order to get new customers | order to understand the market of the | of the market (advantages for leaders | Make advertising on the financial media (magazine, news papers...) in | western state that have a different | Internal rivalry buyers and suppliers | order to target a segment that have high income and asset to invest | demography (different insurance depending| | Forecasting all the marketing and communication budget |(managers, directors, institutions...) | on the state(natural disaster) |

Bank and bill pay online customers present the most | To hire a good communication manager to improve the visibility | | interesting profiles (high income and lots of investable| Propose investment solutions in order to propose high yield products | | assets) |(for institutions and high income) | | | Improve more and more the quality of services given by the call | | | centre to customers | | THREATS | | Impact of the American government with the deregulation | | | of the market (advantages for leaders | | | Internal rivalry buyers and suppliers | | | Forecasting all the marketing and communication budget | Improvement of the quality of the web platform in order to propose | Invest in getting its own ATM system in | | Bank and bill pay online customers present the most | safe services | order to avoid reimbursement and do | | interesting profiles (high income and lots of

investable | Improvement of the back up system | economy in long term keep
doing its | | assets) | | strategy based on low costs | | People are mistrustful
with bank on line | | | | | |

Even if we could suggest many recommendations, we would choose the SO strategy: the company has to reinforce his strengths as the market can involve positively and it can really propose a competitive advantage compare to its competitors based on the low prices of its products. Nexity would need to be focused on improving its marketing and communication but as well the quality of the websites to win the trust of customers.

Conclusion As one said in this paper, Nexity bank has many strenghts which allow it to be one of the learder on the market. Moreover they apply correctly the blue ocean strategy which allow them to generate more profits and to count more clients, but senior executive can not stay on these basis. If they want Nexity to be the number one into this business they have to improve their capacity of attractiveness towards potentials clients.