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Vaulting to Value: Valuing Bank Branch Properties

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Today's turbulent financial and real estate markets present challenging issues in valuing bank branches, which are one of a bank's most important assets in retail operations. The number of commercial banks and saving institutions has dropped by nearly 50 percent over the past 20 years, from 15,158 institutions in 1990 to 7,830 in June of 2010.[1] Of the existing banks, 829 or over 10 percent are listed as problem institutions with 139 having failed this year and 140 failing in 2009.[2]

Despite the consolidation in the number of institutions, the number of bank branches has increased dramatically from roughly 86,400 in 2002 to a high point of 99,000, in 2009. However, in 2010, 925 more branches closed than were opened; this was only the third year since 1934 that there has been a decline in the number of branches; the other two years were also during recessions in 1982 and 1992.[3] As bank consolidations continue, some institutions will be faced with how to utilize or dispose of their surplus branches. The value of a branch that can be used by the parent bank or another lending institution generally has a significantly higher value than one that must be allocated to an adaptive reuse such as professional or medical office.

The continued consolidation of the banking industry, the number of troubled or problem banks, and the decline of the number of bank branches has some industry analysts predicting the demise of the bank branch. A 1995 Deloitte and Touche LLP published report, *The Future of Retail Banking, A Global Perspective*, predicted that half of the traditional retail bank branches in the U.S. would disappear over the next five to ten years due to technology and increased competition; however, as noted above, the number of branches actually increased dramatically. Although underestimating the continued demand for branches, the report did accurately predict important trends such as the rise of digital transactions and banks focusing more on high-profit clients and services.[4]

A September 2009 American Bankers Association Survey of Consumer Banking Preference marked the first time that online banking was ranked higher than any other method of banking, pushing bank branches into second place. Another element of online banking is mobile banking, fueled by the use of smart phones and iPad-type devices, which appeal particularly to younger bank customers. Just released this year is JP Morgan Chase's mobile iPhone application, which enables account owners to quickly deposit a check from their smart phone simply by taking a photo of it.[5]

Despite the technical advances, many industry analysts like Steve Reider, president and CEO of Bancography, believe that the branch bank is here to stay and will remain a critical part of the retail banking operation.[6] Many bank analysts believe that while technology is an integral tool in the profitability of banks going forward, it cannot replace the brick and mortar location and face-to-face interaction that the bank branches can provide. However, technology does allow many of the high-cost and low-profit tasks associated with retail banking to be done much more efficiently and cost effectively. Thus, banks will try to redirect more of their these activities, such as basic deposits and withdrawals, to automated systems such as ATMs or online banking, and leave the larger and higher-profit transactions such as loans, CD purchases and retirement planning to bank personnel.

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[1] FDIC, June 30, 2010.
[2] AP Business Writer Marcy Gordon, Oct. 23, 2010.
[3] American Banker, A Debate Reopens as More Branches Close, Aug. 25, 2010, by Matt Monks.
[4] The Future of Retail Banking: A Global Perspective, Aug. 14, 1995. By the Financial Services Consulting practice of Deloitte & Touche LLP.
[5] No More Banks Deposit Your Check With an iPhone by Michael Suen, July 2, 2010, published in Geek System.
[6] Bancography interview, June 2010.

With so many banking functions being done electronically, the bank branch of the future will look different from what is required today. According to bank expert, Von W. Moody III of Thomson Reuters, traditionally a typical bank branch site averages 1.25 acres and a typical branch building ranges from 3,800 to 4,500 square feet. Moving forward, newer bank branches will get smaller, ranging from 1,800 to 2,400 square feet, with fewer teller lines, smaller backroom work areas, smaller vaults and safe deposit boxes, and fewer drive-through teller lines. Bank branches currently require a high parking ratio of approximately one space per 100 square feet of building area. As the size of bank branches gets smaller so will the land area required for parking and building footprint.

Bank branches are generally located on very valuable corners and out-parcels of shopping centers and cost $500–$650 per square foot to build. Thus, reducing the size of bank branches by 50 percent would have a significant impact on facilities costs and allow for in-fill locations on smaller parcels. What will not change is the importance of a bank's location. A bank branch is not typically the ultimate destination for a consumer, but merely another stop in a long list of daily errands. As a result, branches located in areas central to other errand locations are very desirable; with the most coveted positions being at the main entry to a neighborhood shopping center anchored by the dominant grocer in the market.

However, in the near term, new construction of bank branches will be limited. Banks looking to expand will have numerous vacant branches available to purchase and thus will not need to spend funds on costly new branch facilities.

One exception is JP Morgan Chase, which acquired WAMU. Many of WAMU's bank branches were located in-line in retail strip centers. JP Morgan Chase is moving those branches to more traditional out-parcel locations, either within the same shopping center or in close proximity, which allows them to increase market share while maintaining the existing deposit base. This is similar to the trend of the national drug stores such as Walgreens and CVS who moved from in-line to out-parcel locations 20 years ago.

These excess bank branches will achieve their highest value if they have good visibility, are well located and they are able to be used by another banking entity. A review of bank branch sales from 2007–2010 indicated that bank branches sold for continuous use were on average 3,376 square feet and sold for roughly $400 per square foot. In contrast, bank branches that sold for alternative uses during the same time frame averaged approximately $200 per square foot. Further, a review of national brokerage sites illustrates a downward pressure on the pricing of bank branches due to the increased number of vacant branches, and some prices were less than $109 per square foot.

A major impediment to selling bank branches for alternative or adaptive uses is the lack of financing and the overall lack of demand by alternative users. Alternative users are mostly in the form of small business owners and include realty companies, medical offices, dentists, attorneys, boutique retailers, restaurants, accountants and small used car dealers. Nearly all of these small businesses have been negatively affected by the current economy, creating a lack of capital and market demand to justify expansion or relocation of their business.

In some cases, the value as a bank branch is less than the value of the underlying land and the highest and best use of the site is to redevelop it. However, in the current economic environment, most retailers that compete with bank branches for prime commercial sites, such as fast food restaurants, single-tenant small box retailers and self-service gas station convenience stores, have scaled back their expansion plans. Thus, if a surplus branch is not marketable as a retail banking facility, its value is significantly affected.

One potential area for savings is real estate taxes on vacant branches. Property assessors generally assess a bank branch at a significantly higher value than an alternative use. Challenging an assessment and demonstrating that a surplus bank branch is no longer viable as a retail bank branch, may result in lower assessments and real estate taxes.

In conclusion, the consolidation of the banking industry will make available numerous vacant bank branches, which in turn will allow banks to expand their retail-banking network without the heavy cost of new construction. Access and visibility will continue to be critical, with proximity to destination points such as grocery-anchored shopping centers being favored.

The bank branch of the future will likely be smaller and more technologically advanced, and will reflect the shift of high-cost, low-profit banking transactions to ATMs and online banking while encouraging high-value transactions such as CDs, loans or retirement planning to be done in person with the branch personnel. Branches that can continue to add value as a retail banking location will have a significantly higher value to the banking community than less well-located facilities that more likely will be converted to an alternative use at a significantly lower value.

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