

Comments on **“The Welfare Consequences of ATM Surcharges: Evidence from a Structural Entry Model”**

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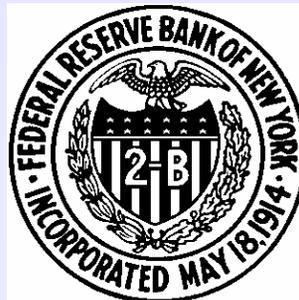
Federal Reserve Bank of Philadelphia

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James J. McAndrews

Federal Reserve Bank of New York

Research and Statistics Group



Significant assumptions of the paper include

- No differences in interchange fees in IA and MN
- No sunk costs to ATMs
- All ATMs are shared
- No search by consumers for ATMs
- No firms with multiple ATMs
- No banking relationships
 - No differential surcharges for depositors and non-depositors
 - No strategic “depositor-stealing” motives for surcharges



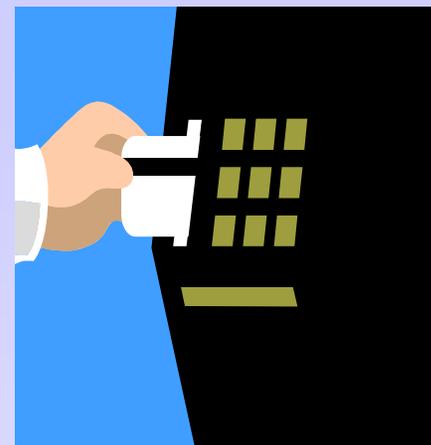
Simple Economics of Foreign Fees and Surcharges.

Consider a monopoly bank in a closed county market with two locations.

No incentives to impose foreign fees.

No incentives to impose surcharges.

- Zero marginal cost of transactions.



Consider a duopoly banking market.

Each Bank will impose foreign fees

- *Sharing agreements involve interchange fees, so the bank must recover those costs.*
- *Wants to encourage use of fixed cost facilities.*

Each Bank will impose surcharges on non-depositors

- *No other way to charge beyond interchange (and double margin).*
- *Strategic motive to steal (attract) depositors.*

Double-marginalization and deposit-attracting surcharges at existing ATMs are welfare-reducing



More on surcharges:

Three motives for surcharges:

Outsiders (tourists, and business travelers)

**“Walking-around” demand of local non-depositors
(may differ by demographics; elderly and minority
populations predict surcharges)**

**“Depositor-attracting” (especially important for
immigrants)**

**Gowrisankaran and Krainer consider variations in the
walking-around demand.**



Banking structure can affect walking-around demand:

Small (single-office) banks will impose lower foreign fees than larger (multiple-office) banks because their depositors do more walking-around away from the single office.

More single-office banks, more walking-around demand.



Banking structure can affect benefits of depositor-attracting surcharges

More concentrated banking markets have a lesser incentive to attract depositors (as “own-bank” ATMs are nearby).

The more concentrated is the market, the less is the depositor-attracting motive.



In sum, if there are systematic differences in the banking structure, or in migration rates and demographic elements, between MN and IA, then the natural experiment is not as clean as one would wish.

The first difference to be discussed is that in the banking structure of the two sample areas. Iowa has a greater preponderance of multi-office banks, and a significantly greater concentration of deposits.



Summary of Deposits for border counties of Iowa and Minnesota

Deposit offices include full-time facilities of commercial bank and thrifts

	Iowa		Minnesota	
	<i>total</i>	<i>per county</i>	<i>total</i>	<i>per county</i>
# of counties	21		11	
HHI *	1660		1325	
Banks	106	7	76	9
Branch offices	226	11	115	10
	<i>total</i>	<i>share of total</i>	<i>total</i>	<i>share of total</i>
Multi-office Banks **	64	60.38	26	26.32
Deposits in multi-office banks (\$1,000)	5,211,483	76.57	1,369,753	46.94

* The deposit-weighted average of county-level HHI (Herfindahl-Hirschman Index)

** Banks with more than one branch office in the area of interest for each state



These differences can affect the policy exercises.

First, the Minnesota, single-office banks, are likely to post lower foreign fees, boosting the walking-around demand for their ATMs relative to Iowa.

Second, the greater concentration of deposits in Iowa are likely to be correlated with lower surcharges.

So the pricing experience in Minnesota may not accurately predict how surcharges would be set, and therefore, how much entry would occur in Iowa.

Bottom Line:

Entry response to allowing surcharge might be less in IA than in MN, resulting in an overestimate of the benefits of surcharging.



Age distribution and change in population looks similar in the two states.

	Pop Change 2000 to 2004 as % of total pop _2000	Over 65 as a % of total population _2000
Iowa Total	-1.89%	18.51%
Minnesota Total	-1.61%	19.58%



Sharing of ATMs

One issue that would be important to understand is the value to consumers of sharing of ATMs among the depositors of different banks, and how much of the benefits accrue to local sharing, and how much accrue to the sharing of distant ATMs.

Can the authors' approach examine the welfare benefits of sharing?



Suggestions

Reduced form

Add some banking-market features to the estimations.

Follow-up study

It would be fascinating for the authors to follow-up their study with the actual outcome in the years since the change in policy to allow surcharging in Iowa.

