ARE YOU BEING SERVED?

As the popularity of online banking grows at an ever increasing pace, retail banks and other financial institutions with costly branch networks have only a five year window of opportunity in which to turn the branches into profit centres. Chris Gentle and Sebastian Cohen look at how this can be done.

Financial institutions that own retail banks are facing a major challenge. How do they re-invigorate their franchises? As the retail market matures, many banks are struggling to grow their customer base and their revenues.

With intensifying competition driving down prices and increased switching between providers, customers in the United Kingdom are more price-sensitive and less loyal than ever before. Retail financial institutions are struggling to connect with their customers. It is not enough simply to acquire customers with an attractive new rate. Banks must now work hard to retain customers, generate more revenues from them and increase the number of financial products sold to each individual. Cross-selling additional products is also significantly more challenging when customer loyalty is lacking.

To address these issues Deloitte has undertaken a major research project based on a consumer survey of 1,000 UK adults, in-depth interviews with key influencers in the retail banking market, and a series of in-house focus groups. This builds on previous research - Bring Back the Branch, Retail is in the Detail and Loyalty Quest.

New thinking is required if banks are successfully to re-invigorate their retail proposition. Our conclusions suggest financial institutions should seek to change the basis of competition by creating a value-added proposition that attracts and retains customers by leading on service rather than price. To reconnect with customers, the fresh proposition should be based on the principles of convenience, value and service. In the battle for customers – and their hearts and minds – the branch will be critical.

Levering the branch to change the basis of competition

New thinking is required. Financial institutions should seek to change the basis on which they compete by creating a new proposition that attracts and retains customers by leading on service rather than price. Such propositions are tasked with reducing banks' dependency on price-based competition by providing customers with a higher quality service. In detailing a new vision of banking, the research indicates that branches have a significant role to play and will be a critical channel for delivery of a new customer-centric offering.

Locking in value through the branch

So what are the key elements of such a proposition? Based on experience in the United Kingdom and around the world, Deloitte has identified convenience, value and service as the vital drivers of consumer behaviour in financial services. These are detailed below:

Convenience: when choosing a bank, convenience factors (such as location and accessibility) rate highly with customers. Increasing the accessibility of each banking channel is key to creating greater convenience. Some US banks are beginning to compete on convenience by changing branch opening hours to meet customer requirements. First Community Bank opens selected branches from 07.30 to 18.00 and Commerce Bank keeps all stores open 361 days a year. Knowing the specific demography of a branch's local community is vital. Commuting customers typically require earlier opening hours while rural communities prefer later opening times.

Value: customers are more likely to stay with a bank if they pay a price they deem fair for the quality of banking products and services they receive. Customers expect to pay an appropriate price for services, not necessarily the lowest price. Because Commerce Bank trades on its strapline as 'America's most convenient bank' it has less need to offer market-leading deposit rates compared with competitors.

Service: superior service creates loyalty and deeper customer relationships. Conversely, a lack of appropriate

Figure 1: Core elements of the retail proposition

Customer experiences	Customer decisions: Choose	Stay	Expand
Convenience	High		Low
Value		Medium	
Service	Low		High

Source: Loyalty Quest, Deloitte Development LLC, 2005

service can destroy those relationships. A differentiated service in the future is likely to comprise offerings tailored more closely to the lifestyle of customers. Evidence suggests that direct channels still fail to deliver the right level of service for most customers. Improved service takes many forms. HSBC's Matchmaker system uses a concierge who directs customers to the staff member best able to deal with their enquiries. This helps to reduce queuing times in the branch. Creating a cultural change in which branch staff can 'solve the problem' is likely to become increasingly important. Again Commerce Bank is held up as an example – its customer promise is simply 'ask, listen, solve.' For a summary of the core elements in building a fresh retail proposition, see Figure 1.

Each proposition should be crystal clear to the customer, and should differentiate the organisation based on a combination of these drivers. Deloitte's research suggests the branch is likely to remain best placed to deliver the right mix of convenience, value and service and is therefore the key channel through which banks can turn the tide against the commoditising forces of direct channels.

Branches to lead the change

Analysing consumer research into branch usage and attitudes, it is clear that the branch is key to delivering the new proposition as it is the primary channel through which service and sales is delivered to the customer.

Figure 2 shows that nearly three-quarters of consumers have a preferred branch they regard as their 'regular.' It also shows the majority still see the branch as the main channel for accessing banking services. Almost two-thirds of people would not choose a service provider if no access to a branch was offered. Banks also need to exploit the fact that fewer than one-in-ten of the population never use a branch. Clearly, the branch remains instrumental in delivering service. The challenge now is to modify the behaviour of customers to increase footfall into the branch, create an excellent in-branch customer experience and improve the propensity to purchase.

Branches are also instrumental in the sales process. The consumer research revealed that nearly 90% of respondents arranged their current accounts (held with their main service provider) at a branch. In addition, 76% of cash ISAs and savings accounts held with the main service provider were also arranged in-branch. This emphasises the revenue-generating power of the branch network, particularly as a base from which to cross-sell.

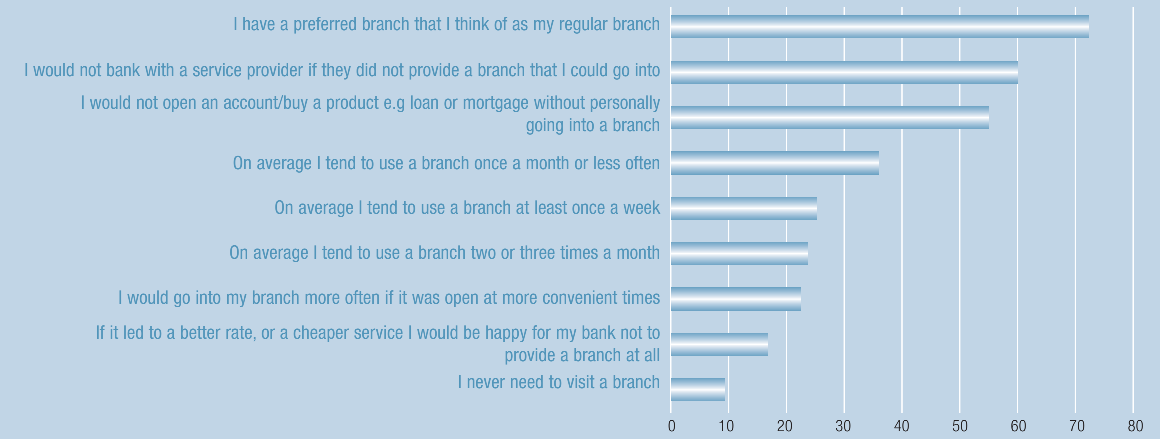
To improve the quality of service and sales by creating a unique and differentiating mix of convenience, value and service, retail-based finance institutions should therefore look to their branch networks.

Are branches ready for the challenge? It won't all be plain sailing

However, there are obstacles to achieving the vision. Viewed as little more than cost centres for many years, branches have suffered from underinvestment. In the late 1990s Britain's top retail banks reduced their networks by one-third as they built up direct banking capabilities. And such a lack of investment has left an unhelpful legacy of poorly located and maintained branches, and de-skilled, de-motivated staff. In addition a third of customers now predominantly bank online with just a quarter using a branch once a week. The volume of footfall flowing through the branch is therefore declining and customers are using branches less frequently.

Many branches are struggling to perform – let alone to deliver on convenience, value and service. In fact, several interviewees suggested that their branch networks are far from optimal in this respect. Their branches have struggled to keep pace with population shifts in micro-markets, leaving some increasingly prosperous areas underserved and others over served. Branch networks

Figure 1: Core elements of the retail proposition



Base: 1000 UK adults, ages 18 and over. Source: Deloitte Research UK/BMRB 2007

have also found it similarly difficult to respond to changing footfall patterns in the high street.

The costs of running more than 13,000 branches in the United Kingdom are estimated to be around £10.5 billion per annum, generating revenues of £13.7 billion. This suggests two things. First, the network can still carve out a profit, and therefore should not be written-off just yet. Second, cost to income ratios at the branch can drag down the overall performance of the retail bank. As branches essentially have fixed costs, banks must improve cost to income ratios by increasing revenues. This is well worth their while. A 10% improvement in revenue could drive an increase in branch profitability of up to 40%.

> Creating a cultural change in which branch staff can ‘solve the problem’ is likely to become increasingly important.

Turning the branch from a cost centre into a powerful income-generator and the focal point of an enhanced service is a significant challenge. It requires nothing short of transformation. Succeeding in these challenges should sift the leaders from the laggards in the retail-banking arena.

Branch banking transformation - six disciplines

A walk down any UK high street reveals banks are being outgunned by retailers in the sophistication and relevance of their customer propositions – further raising the bar of consumer expectations.

The research identifies six disciplines that can help retail financial institutions achieve a fit for purpose branch network. Under each of these disciplines three action points are highlighted that should help transform branches – forming a definitive check-list for transformation.

The six disciplines are: people strategy, customer service process design, property strategy, branch economics, product development and security and risk planning.

People strategy: is the glue that holds together all aspects of transformation. For instance, investment dedicated to increasing the level of customer traffic entering the branch is likely to be wasted if bank employees are not empowered to deliver higher quality service. The key people changes to make are:

- Reward service provision, not just sales performance.
- Create long-term employee incentives to create deeper customer relationships.
- Reassess the employee profile to more closely reflect the local demography.

Customer-service process design: designing the right customer-service process is crucial if banks are serious about avoiding commoditisation. Banks should make more time for excellent service and ensure that precious staff time is delivered to customers when they value it most. Specific action points include:

- Understand customer behaviour across the channels
- Adjust the channel mix to free resources for more service
- Tailor services to the needs of the local branch/demography

Property strategy: well-located branches give customers convenient access to services and can capture new business. And good branch design can improve the customer experience. The following recommendations should be taken forward:

- Agree a portfolio-wide approach to change (site disposal, acquisition and refurbishment)
- Prioritise branches according to a location/business strategy
- Move to a retail design where appropriate for the location

Branch economics: sales strategy is typically driven from national targets around specific product-pushes across the whole network and the in-branch sales process is typically fragmented. This has led to blunt demotivating sales targets, poor quality sales leads and low conversion rates. Banks should consider:

- Adjust the channel mix to improve the quality of sales
- Improve the sales process in the branch
- Create local (community-based) sales targets

Product development: Banks are seeking to standardise and simplify products to make them easier to manufacture, distribute, process and package together. Early attempts have had moderate success in bundling products together but making the product mix relevant is a key challenge. Recommended action points include:

- Use branches to inform the product development process
- Create in-branch conversations around product needs
- Ensure products and packages are appropriate at the micro-market level

Security and risk planning: Security has risen up the regulator's agenda and the media spotlight is increasingly focused on exposing security breaches in banks. Branches need to cope with a number of developments such as the move to open plan design, which has brought with it potentially easier public access to data. The following processes should be put in place:

- Improve branch 'housekeeping' around security measures
- Regularly review security against benchmarks
- Replace manual procedures with auto-control processes.

Each discipline is mutually reinforcing. Those that execute only partially on this agenda are unlikely to create a compelling proposition that can retain customers in the long term. In order to win with branches, banks need to complete a fully executed transformation across all six disciplines. As a result, the branch network can become not only a valuable asset, but the leading channel that underpins a new customer experience based on the principles of convenience, value and service.

The clock is ticking…

Banks should feel a sense of urgency. Retail financial institutions have around five years in which to change branch usage and the propensity of customers to buy additional financial products. The new proposition must be established before direct banking channels dominate and the customer relationship becomes merely virtual - altering the market dynamics beyond recognition.

Conclusion

Avoiding commoditisation, improving customer retention and creating cross-sale opportunities are key goals in growing revenues and when revenues grow so too can shareholder value over the long-term. To achieve these objectives a new proposition is needed – one based on convenience, value and service and the creation of tailored products and services. To drive future shareholder value, fresh thinking is required. Winning banks are likely to be those that create a cost-effective proposition that can enthuse customers, pull them out of their inertia and give them a memorable experience.

In delivering this vision, it is clear that banks should mobilise a multi-channel strategy – carefully using the Internet, telephony, enhanced ATMs and branches to support the delivery of a fresh proposition. However, the branch is in a far better position than direct banking to create deeper customer relationships and superior service. Our research suggests the branch, therefore, is the key channel to carry forward a new value-enhancing proposition.

Against this top-down approach, there are some bottom-up challenges to delivering this vision. The lack of investment in UK branches over the past decades has created an historical legacy of underperforming branches, unmotivated and de-skilled branch staff and inefficient processing. The cost of maintaining and turning around the branch network to make it perform and rise to the new challenge is therefore significant. The huge cost and revenue sums involved make this a burning issue for retail financial institutions.

While many banks have set out on a path to branch improvement, arguably few have embarked on total transformation. Simply refreshing the brand and refurbishing the branch network is unlikely to be enough. Only a unique, differentiating and compelling proposition is likely to succeed. Financial institutions that consistently execute across all six key disciplines for branch transformation are likely to win with branches. ☐

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