The key to real industrialisation in banking
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We provide support to our international and national clients in their endeavours to tackle a wide array of business concerns and to fulfil their overall strategic ambitions.

We believe that people in organizations are capable of achieving far more than they think is possible.

We believe that connecting HEARTS and MINDS of people is the distinctive factor in achieving lasting effect and “passionate” work environments.

We believe that knowledge and experience is a necessity, but the connection with the human factor will make the difference.

The art of thoroughly compassing our client’s demands, constantly adapting to their unique and local cultures anticipating the changes and challenges they are facing. These are our unique strengths and at the same time the basis of our unfailing commitment to our clients.
EXECUTIVE SUMMARY

The current pressure on costs in the financial industry, driven by the economic crisis as well as increasing regulations, has a significant impact on the critical mass necessary to run certain banking activities, as well as on the degree of digitalisation.

In this context banks aim to further optimize their operating model, continuing the shift towards industrialised banking that has been accelerating for a few years now. But in doing so, banks face barriers they struggle to break.

To move a significant step further towards industrialisation, top bank managers need to consider four key success factors:

• A rigorous and long term oriented management of product portfolios, covering the full life cycle of banking products. This is the best way to avoid hidden non-profitable product offerings and optimise processes in a more industrialised way;

• Mastering the client desire for personalisation. Creating the ability to differentiate from a customer perspective, as opposed to operational efficiency, has become a real competitive advantage;

• The industrial management of information: the rise of digitalisation requires an ability to meet high expectations from customers in terms of a holistic view, speed and quality;

• Anticipating and controlling the requirements of changing and increasing regulations.

Throughout these four key success factors, one topic in particular deserves the greatest attention from top management. An active promotion of cross-organisational management and initiatives will avoid the formation of organisational silos, and the need to building bridges between departments and business units.
WHY THIS STUDY NOW?

For several years now, banks have had to face three main issues: cost reduction, critical mass changes, and the rise of digitalisation.

Banks have been dealing with cost reducing solutions since the beginning of the crisis in 2008. In our role of business advisors, we have observed the major question raised by top managers: how can I cut costs intelligently and efficiently? This is increasingly becoming the most critical issue not only for operational managers, but also for commercial functions like distribution and marketing. In a word, the entire bank organisation has been affected. We believe this is not only due to the need to react to negative business forecasts, but also – and in some aspects, primarily – to a new demand from the customer community.

Changing the awareness about processes, operations, costs, and investments, is basically driven by volumes and dimensions. The ignition point of a spontaneous effort to radically redesign the “how to”, excluding external impulses of new or incoming regulations, is usually determined by size. Banks with a wide physical coverage of the distribution/commercial network have started acting as factories. In the EUROGROUP CONSULTING study “The onset of banking factories” (2010), we envisaged this perspective, concluding that critical mass of transactional volumes is the key factor to force shifting to this new paradigm.

Furthermore we are well into the digital era. The line between enterprise and consumer solutions has never been as thin as today, and the future seems to bring even more convergence. This is driven by sophisticated customer expectations, not only from younger generations. Add to that a certain view on services which are no more perceived as valuable, some of which are traditional banking processes. Thus the digital paradigm is both a threat and a big opportunity. Banks must definitely exploit the best of what new technology is offering to foster their current operational model toward a new comprehensive one.

Designing an “industrialised” banking model is the answer around which a lot of energy has been spent by a number of banking groups and financial operators to solve their operational issues. Nevertheless, outcomes show that something is lacking or missing in the ways to go further, due to a variety of reasons. It is now time to focus on these reasons and open ourselves up to potential solutions.
BECOMING INDUSTRIALISED

What are the distinctive factors of an industrialised model? As a starting point, conducting an activity in an “industrial way” means being “organised to handle large volumes”. In a practical sense this further implies that constant concerns include:

• Searching for productivity. Productivity improvement in banks relies on continuous process optimisation.

• Minimise costs. Big volumes in a quite labour intensive and strongly production-oriented environment may lead to a wide range of hidden costs. Above this the sheer number of operational sites, as well as their size, is in itself a cost issue.

• Striving for a permanent zero-defect production. Best possible quality in the operational processes comes from straight but flexible processes which allow for proper monitoring of each phase. This is also bringing important benefits on the operational risks management.

If we look to other market segments than banking, the best applications of these basics can be found in the natively industrialised sectors such as automotive, but even more in consumer devices and goods. These sectors are subject to a massive production once the product design phase is over. So far, almost the entire set of methodologies and tools with the purpose to optimise activities and costs are born in other industries than banking. Some examples that have been selectively imported by large banking groups are Business Process Reengineering or Integration (BPR/BPI), Lean Six Sigma and the related Value Stream Mapping approach, as well as Business Process Outsourcing.

The outcome for banks has been some important achievements: inventive and straight processes, which are almost fully automated; banking factories, some of which under a cooperative operational model among a group of competitors; many non-core activities such as documents and material handling, general contract management, facility management, etc., have been outsourced in order to reduce related costs as well as move from a fixed to a variable cost structure; finally, a strong effort has been done on HR-management, given that a significant part of the gross margin is absorbed by payrolls.

Through our experiences with clients throughout Europe we have identified some major trends to cover the cost issue. For instance, a large European universal banking group launched several programmes in the last five years and thus was able to cut its cost to income ratio by nearly half.
There is definitely an important tendency in the European financial sector to move towards industrialised operational and organisational models. Nevertheless, something is still missing. Considering all initiatives around cost, productivity, quality, etc., the effects remain far from what has been expected. Clearly, banks face a number of difficulties preventing them from making significant progress.
FOUR KEY SUCCESS FACTORS

To move a significant step further towards industrialisation, top bank managers need to carefully consider the following four key success factors:

1. A rigorous and long term oriented management of their product portfolio
2. Mastering client desire for personalisation
3. The management of information in the new era of digitalisation
4. Controlling the impacts of a changing and increasing regulation

KSF1: Managing obsolete stocks in the product portfolio.

As in many other industries, banks usually manage hundreds of products across business units as well as customers. For instance the commercial success of a financial product is not necessarily linked to a particular campaign, leading to some products being sold for a long time, no matter whether they are effective or not.

There are two characteristics which are highly distinctive in the management of financial products and services: lifecycle and structure. Normally, the lifecycle is quite long, and in most cases the structure is difficult to move to an updated and smarter version.

In the high-tech consumer market, which is largely industrialised, product dynamics are dramatically subjected to short term versioning. Furthermore, after a pre-determined period, manufacturers simply stop maintaining old stock, forcing the market to substitute the obsolete equipment. And in the automotive industry, maintenance is a product in and of itself, with a specific revenue stream. Old cars are normally not maintained by the manufacturer unless the customer pays a high price.

For banks, these industrialised practises are not applicable at all. Obsolete products are often kept operationally alive, even when they are not sold anymore. This is because they are still used by some clients, often just a few. Regardless of all costs involved, banks must maintain a whole set of processes and IT at their own cost. They must also keep an eye to potential regulatory burdens. Especially for banks, product management matters.
A first assessment of product portfolio is possible using a simple matrix, combining the assessment of:

- The profitability of a product
- The lifecycle of products

Basically, the life cycle of a product can be divided into three phases: design, launch, and manage. The last period can last for a long time and will eventually finish with the termination of the product.

The assessment of the profitability of a product does not mean a mere margin analysis, but also implies other aspects, which must be considered in the long term:

- Expected level of quality
- Impacts of processes in front and back office
- Information and communication technology platform
- Risk evaluation, such as legal, operational, and compliance

Ideally, the life cycle of all products should remain on the profitable left side of the matrix. In reality, the cases 1, 2, and 3 described hereunder occur all too often.
Managing their product portfolio, banks usually face following issues:

1. Often the design process of new products does not embrace all components of the cost of a product, especially in the medium and long terms, while focusing too much on marketing and IT costs. What seems to be a good idea might not in fact be profitable.

2. The second case concerns new products where an unfavourable commercial story is soon revealed – the necessary volume is not met, which ruins the initial business case. In an industrialised environment this should immediately correspond to an effective remedy: new design, transformation, a new commercial approach - whatever it takes to bring the product back to profits.

3. Finally, there are the old products that for many potential reasons eventually turn out to carry costs too high compared to the income generated. Usually these products cause high complexity in the overall information architecture. As related IT modules are often old they lack available updates and maintenance, as well as not being engineered to be readily converted into new building blocks. Significant investments are required to remedy this situation. These products need to be terminated.

Any combination of these different cases causes banks to accumulate unprofitable and often old products which are not sold or used much anymore. These are still kept due to a lack in proper cost analysis or to the reluctance of banks to terminate products still in use by some customers.

To adhere properly to the industrialised paradigm, it is imperative that banks accurately rethink their entire product design processes and rules. Management should focus not only on short term profitability, but should also give enough room to the shutdown design, i.e. how to manage products once they have turned into obsolescence.

The main points to be considered are:

- It is evident that starting as early as the design phase, a sound and effective collaboration among all affected departments would prevent not only launching non-profitable products, but also prevent building up an obsolete, expensive and complex product stock.

- Product portfolio assessment needs to be done regularly, as a permanent control.

- All risks must be taken into account: legal and regulatory constraints, brand and image, and single or even massive claims. This implies both an adequate economic coverage and a contingency plan, the latter being often underestimated.
• Thorough and comprehensive marginal cost analysis in order to
determine whether it is more appropriate to keep the stock or to
terminate it.

• If termination is the answer, the migration plan to push customers
towards alternatives needs to be designed. This normally requires a
budget for customer incentives, e.g. a new product offered at a very
attractive price for an adequate time. Of course, there is the issue of
change management and client interfacing, particularly in a multi-
channel environment. The distribution network needs to be involved.

**KSF2: Mastering the client desire for personalisation**

People are increasingly behaving as citizens of one large global commu-
nity. Thanks to the massive penetration of digital devices people are
always connected, always informed, and always advised on best trends
and practices, or on things to avoid. All this is presented in a highly
personalised form. In line with this general trend, the banking customer
is increasingly looking for more personalised and tailored products.

At a first glance, this looks contrary to the pursuit of standardisation and
homogenous production, for which all industrialised organisations are
striving. But we feel the solution is a step beyond this appearance. The
real dominant factor in the customer expectation is experience, and this
means service.

Banks must understand this new mentality, and respond with a mix of
product design and operational innovation. Bundling complex financial
products, which before the crisis was a major source of income is no more
the Holy Grail. This is particularly true in the digital era, when easy-to-
compare features are considered mandatory. The new banking product
packaging must include the right service, and present the customer with
a special-looking experience, as if it were really done for his or her needs.

A common example is when a customer is buying a house. Merely selling
a loan, whatever financial trick goes with it, might not fit with the
customer vision of finding a home for his or her family. What matters is
matching the offering with the whole customer experience, though a
transparent combination of easy components which will progressively
accompany the customer through the purchase of a home.
Thus, depending on market expectations and on technical issues, banks can adopt two options:

• Offer as much as possible in a simplified, easy and standardized product mix. Bundling is done through customer oriented services, which are not affecting the products structure in any significant way. Tailoring can be done on the service side, depending on customer profile and needs:
  - Provision of easy to handle services, with low or none impact on the product – such as recharging a pre-paid credit card, moving of account coordinates for the payment of a personal loan, or utilizing digital channels.
  - Personalised, direct and high-quality relationships for highly profitable customers and products, provided through the whole distribution model using bank advisors.

• Design a standard core part of the product, not to be subject to modifications and common to all identified versions, and manage the personalisation of the offer to the customer through a set of variable criteria. Before adopting this model, which is inspired from best practices of highly industrialised trades such as automotive, it is important to ensure that the entire operational value chain has the required capabilities. Specifically IT legacy system must be engineered to manage this product structure, and particularly the variable parts.

The automotive industry perfectly illustrates the combination of industrialisation and personalisation. Cars of a given automotive group are designed around a core of technical components common to as many models as possible. This includes parts like platform, motor, electronics, internal fitting, etc. For instance, the Volkswagen Group has developed a platform, called MQB, which is used by more than 40 models from its different brands: Volkswagen, Audi, Skoda, SEAT.

The latest trend is to let the client, in the purchasing phase, choose not only options, but also the colour and design of several external outfits, which are marginal in terms of cost per unit.

In 2009, Citroën launched the DS3 model emphasizing the fact that one can personalize almost any component, thus making every car unique.

Another example comes from the computer business, where, despite a standardized structure, one can choose several components to adapt the computer to his or her requirements.
KSF3: Managing information in the new era of digitalisation

The fast and endless proliferation of digital devices and channels, like smartphones and digital television, is radically enhancing users’ expectations of reliable information. It is not only a question of volumes, but also one of speed – information must be provided as fast as possible, if not on a real time base. Banks need to consider the fact that in this new world they have become one of the most important information providers. They must face this new challenge, not only towards the institutional side but also in the daily transactional life of a consumer. For instance a credit card user wants real time access to accounts, in order to be able to manage limits optimally – this must be provided through a smart service.

How can access to information be accelerated while including more channels and improving quality at the same time?

For a long time, banks have underestimated this point. Many processes are still poorly automated, with a large portion of manual entries. End-to-end processes are not optimized, even when included in an industrialised high-volume environment.

As an example, we have observed that few banks are yet able to provide customers with a complete at-a-glance dashboard of their financial information, such as balance of all accounts, amount of loans, stocks information, and insurance.

Compare with the Telecommunication and Energy industries:

Customers can view their profile within digital dashboards that not only show the real time details of consumption, but also provide effective tips on how to save money through better usage of electrical appliances. These are two remarkable achievements from effective investments in what digital devices can offer. Customer experience has been enhanced while the cost of providing information has been lowered to a minimum. We see both quality and effectiveness thanks to the digital paradigm.

For banks, much is still to be done regarding information management in order to keep up with the pace of customers and the digital revolution. Adopting a “simple” lean approach is most likely not enough, instead banks have to rethink the whole architecture of information exchanges, including front line processes.
Paperless banking, for instance, is a good example of how to achieve several goals using digitalisation in processes. With a mix of easy end user devices, lean process reengineering, and light IT maintenance, an important set of critical pieces of information, like contracts, can suddenly be digitised and easily distributed internally as well as to customers.

A major European bank started a programme of native paperless processes a few years back. The results speak for themselves: more than 95% of customers were migrated within the expected period of time to the new operational model; marketing has acquired or updated the entire set of customer email addresses, to which they address not only transactional information, but also marketing campaigns; some cost typically related to branches and of a significant size in a wide distribution network, such as paper purchasing and material handling, have been radically cut; last, but not least, information quality increased which contributes to lower operational risk.

However, most banks have created highly complex IT systems. These colossal platforms, which are the results of complicated component patchworks over the years, are rarely efficient. Even when they are affordable, they are ticking bombs when viewed from a process digitalisation point of view, as they require a significant amount of changes and adaptations in the IT architecture. Few banks are trying to find a solution because of the high costs involved. While this is certainly true, we still see a radical difference today comparing to past decisions on IT architecture overhauls. When the digital paradigm is a substantial factor, the ROI is often so high that top management of any bank should not avoid considering the required investments.

This implies two basic rules:

- First, internal vision must be oriented towards bold changes and the ability to see the real effectiveness of becoming digital. This means much more than merely installing tablets for bankers
- Second, each investment must have an accurate, solid and consistent business case based on realistic assumptions, which may not only be inspired from marketing trends, even when successful, but also from real examples and best practices.

The digital revolution applied to an industrialised environment requires bank CIOs and COOs to view their operational model less as a static rock, but more as an agile and resilient tree – both solid and elastic at same time, open to accept fast and important environmental changes without any major risks. It is not only a matter of IT. Too often, banks still manage their channels, as well as their business lines, as silos. Bank management has an important role in bringing people and operations together in a more cross-organisational vision inspired by general interests. This helps foster effective cross-departments processes, while closing the link between people – including customers – and IT systems.
KSF4: Controlling the requirements of changing and increasing regulations

For a few years now, there has been a constant flow of banking regulation. Brand new or updated rules are issued frequently, and this will probably continue for a foreseeable time. For European banks in particular, the integration path of the European Union will undoubtedly bring new regulations in order to harmonise banking practices across countries. A lot of work had already been done in the period before this crisis started, when some major regulatory frameworks were put in place – Basel II and MiFid above others. Now this process is even accelerated.

However, banks are still not optimising regulation implementation. They are so fixed on compliance that they spend much of their time trying to adapt activities to the rules instead of developing profitable activities within the rules. It even happens sometimes that a new activity, quite far into the building process, is stopped or suspended before going to market because of the potential impacts of incoming rules in terms of costs and risks.

Most of the time, the issue is not the regulations as such, but the changes – and how to manage them consequently – brought by the regulation. This is a constant challenge for processes and organisation, but also most of all for the IT systems of banks, due to their heavy complexity. This does not facilitate becoming industrialised.

We have been investigating the telecom industry, which is also subject to wide regulatory burdens both common and local, and which is typically oriented to massive production. As explained in the sidebar, telecom firms manage regulatory changes fairly well thanks to a modern IT architecture.

Telecom firms can count on a native digital process. After the transformation of stations from analogue to digital in the late 1990s and beginning of the new century, the entire industry can rely on a massive digital operational machine. With a capacity to handle billions of transactions per second, this infrastructure is run and managed by virtually unattended processes. This allows operators to react to several and frequent changes in regulation with clever data management. For instance, many telecom rules require transparency in the billing processes. Invoices must provide comprehensive details to the customer, segmenting the fees applied for any kind of usage like domestic and international calls, data traffic, and so on. This is quite similar to the interest rate components transparency required in many financial regulations.

Once more, balancing the industrial way versus mandatory requirements requires a modern vision of information architecture and strong automated processes in order to be able to react to regulation innovations in an effective way. Increasingly inspired by customer needs, banks can gain economic and competitive advantages while at the same time fit well into the spirit of regulations.
NEXT STEPS TO REAL INDUSTRIALISATION

Considering what has already been achieved and what is anticipated in coming years, the banking industrialisation step appears inevitable. The way to become industrialised today, compared to five years ago, is more complex due to several factors which are currently apparent on a global scale. In particular customer behaviour and new technology developments impact the increasing demands for data reliability and transparency.

Most of these issues can be addressed by an industrialised business model, but to hold the course banks need to:

• Consistently rely on their own strategy, clearly envisioning how their operating model fits with the new environmental expectations. Of course, client demands should drive the experience to interact with the bank; on the other hand, banks must set the rules and the playing field in which client relations are built, and thus leading the customer experience.

• Respond to the increasing demand of personalisation through a renewed product/process design, with a special attention to product life cycle implications. It is possible to give the customer the perception of personalisation while staying in a strongly industrialised operational model.

• Be more oriented towards cross-organisational processes, thereby committing key people from a wide range of functions in any decision which affects internal assets such as products, information, customer services, etc.

• Study native industrial segments to find inspirational examples, and to apply best practices internally through well-supported, but also courageous, decisions.
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