The Banker's Dilemma
How To Build A Bank

White Paper
December 2014

Polaris Partners

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Bricks? Clicks? Both?

That's the question that bankers are grappling with today – and getting the answer right could be the key to survival.

Begin with the worries:

- Branch networks, the traditional distribution channel, are expensive to maintain
- Younger customers are increasingly happy to do all their banking digitally
- Challenger institutions are slashing distribution and servicing costs by using only digital platforms (their cost-income ratios are said to be about 30%, with traditional retail banks above 50%[i])
- Changing fee structures make it less and less profitable to service lower-value accounts

On the other hand:

- Older customers are doubtful about digital
- The wealthier the customer, the more she demands personal service
- Complex savings and loan products are tough to sell digitally

Picking a way through these conflicting choices isn't easy. For sure, there's no lack of opinion out there: but it's wise to apply a discount to the claims of those who stand to benefit from their "forecasts", and also to recognise that what consumers say they'll do is often a far cry from what they actually do. (As a case in point, recall the pundits' e-book prophecy that "It's the end of books as you know them"; in fact, their share seems to have plateaued out at around 20-30%[ii].)

So, rather than predictions, let's look at some facts:

- RBS and NatWest branches have seen a 30% fall in transactions since 2011. Over the same period, their digital and online banking transactions increased by over 200%[iii]
- Footfall at HSBC branches has fallen by 30% since 2009, with a 10% drop between 2012 and 2013[iv]
- The number of transactions carried out on mobile applications doubled in 2013. Meanwhile, bank call centres saw volumes drop by more than a quarter last year[v].
- Almost 90% of US households live within ten minutes of three or more different banks. 75% have a choice of six or more[vi].
- The average cost of servicing a client in a branch is $4 per visit, while at a cash point it is 48 cents, and using online or mobile channels costs only 4 cents, according to research from Autonomous[vii].
- Spain, Italy and France have 50-80 bank branches per 100,000 inhabitants. Sweden, Denmark and Finland have only about 20 branches per 100,000 inhabitants[viii].

> *"Do you know what our busiest bank branch is in the UK? It's our mobile app on the 7.15am train to Paddington." Ross McEwan, Chief Executive of RBS*

Clearly, some hard thinking is needed about the extent and role of the branch network. Two widely different points of view illustrate the range of possible responses:

First, the "Branches are for dummies" approach.

Atom Bank, founded by Anthony Thomson, a founder of Metro Bank, and backed by City heavyweights, is soon to launch as the UK's first "digital only" bank. For him, "Atom is in the business of data, not the business of banking."

> *"The direction of travel is absolutely clear. Whether it's three years, or five years, it is clear that banking will largely be done on mobile phones and tablets, not in bank branches. Banks need to adapt to this new reality." Anthony Thomson*

Next, the "Branches are essential" approach.

Handelsbank, based in Sweden, disagrees with Thomson: focussed firmly on personal, face to face banking, it had just three UK branches in 2000, and now has a network of 176.

But maybe there's a middle path: the "Branches how and where necessary" approach.

This school of thought argues that banking is a mix of routine transactions, best handled digitally, and complex transactions, best handled personally.

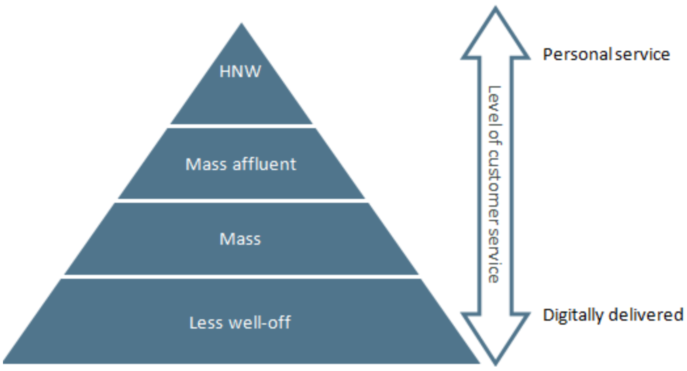
Accordingly, the most appropriate solution is to thin networks out judiciously, using demographics and transaction analysis to determine which should be kept and which closed, while at the same time upgrading selected sites so as to meet the needs of customers who want to discuss their requirements individually.

And there's a further thought: just as some transactions are more profitable than others and therefore need to be handled differently, so are some customers more profitable than others and should be handled differently, too. This leads naturally enough to special treatment at branches, dedicated relationship managers, customised product bundles and all the trappings of personalisation.

first direct is a "telephone and Internet only" bank noted for its outstanding customer service. Despite this, in the 25 years since its launch, it has gathered only a modest 1.3 million customers.

So how to deal with the less profitable accounts? This is more controversial. Some banks have gone as far as charging for, or even withdrawing, facilities from less "economically active" customers. But remember Bank of America's ill-fated attempt to charge for debit cards: this can arouse a firestorm of negative PR, especially where there is a perceived social need to serve the "under-banked".

Perhaps, in theory at least, we would end up with a customer/service structure looking something like this:



From Theory to Practice

So much for the theory. What are banks actually doing? For the most part, they're not following either the Atom Bank or Handelsbank models. Some clearly would like to defer any decision for the moment. Others are focussing on selected segments – typically the most profitable – while introducing with greater or less enthusiasm various elements of digital service.

Around the world, we find examples of a segment-led approach. Citi has become the leading wealth manager in Asia through its fully-featured Citigold service for affluent clients. Banks in Mexico and the Gulf offer lavish in-branch personal attention to their wealthy customers. TD Bank in the North East US states is often cited for its shop-like branch operations which help it garner a disproportionately high share of retail deposits. Similarly, Hang Seng in Hong Kong has focussed on building business through a commitment to communities and easy accessibility – even operating branches in the mass transit system. In the UK, Coutts are experimenting with a 24/7 video consultation service for their upscale customers.

Alongside these sharply-targeted services, branch networks are shrinking: UK banks have closed more than 350 branches in 2014, while Barclays is reported to aim at shuttering about a quarter of its 1,600 locations in the medium-term. In the US, McKinsey says that in 2013 more than twice as many branches closed their doors as opened[ix].

However, closing branches carries risks: the elderly – who tend to be richer – generally prefer to do business face to face. Will Millennials always be wedded to digital? And who wants to be the bank whose customers only have competitor branches to choose from?

Finding that Middle Way

Perhaps the solution is a carefully calibrated mix: a range from "digital only" for the least well-off, through "good-enough" branches for the mass market, to increasingly personalised services as the customer moves up the hierarchy. After all, this would only be to mimic well-established policy with regard to payment cards: entry level through usage-defined tiers through to super-prime.

Clicks? Bricks? Both? You can make a case for all three approaches. But one thing is essential – and not always as visible as it should be: having a coherent strategy.

[i]UK banks axe branches in favour of digital model, *Financial Times*, 24 October 2014
[ii]Global Ebook Report 2013, Wischenbart, http://www.wischenbart.com/upload/Global-Ebook-Report2013_final03.pdf
[iii]The Way We Bank Now, British Bankers' Association, 2014 https://www.bba.org.uk/wp-content/uploads/2014/09/Waywebanknow-final.pdf
[iv]The Way We Bank Now, British Bankers' Association, 2014 https://www.bba.org.uk/wp-content/uploads/2014/09/Waywebanknow-final.pdf
[v]UK banks axe branches in favour of digital model, *Financial Times*, 24 October 2014
[vi]The future of US retail-banking distribution, McKinsey & Co, August 2014
[vii]*Financial Times*, 24 October 2014
[viii]Banking Structures Report, European Central Bank, November 2013
[ix]The future of US retail-banking distribution, McKinsey & Co, August 2014

About the Author
Roy Stephenson, Polaris Director

With more than 20 years of experience in the payment card industry, Roy was previously with American Express, where as VP and General Manager, he launched the highly successful commercial card business in the UK, going on to lead product rollout across EMEA and latterly Latin America/Caribbean.

As a consultant, Roy works with banking and payment card clients around the world, identifying and advising on best practices in customer marketing and relationship management. He has also undertaken assignments in media, utilities, airlines and retail.

He has developed and audited coalition and bank loyalty programmes in the UK, Ireland, the Netherlands, Spain, Canada, Dubai, Kuwait, Australia, Singapore, Greece, Israel, Turkey, Saudi Arabia, Brazil, Chile, Venezuela and Mexico.

Roy has also advised on airline FF programmes, and has been the rewards lead in the MasterCard Advisors pool.

He speaks fluent Spanish, reasonable French and is the author of Marketing Planning for Financial Services (Gower Publishing). He has a B. Com, holds an MA in Management Studies and is a Fellow of the RSA.

About Polaris Partners

Polaris Partners is a young company led by directors with decades of experience as senior managers and consultants. We specialise in helping businesses reach their sales and marketing goals.

Most of our work is in the financial services and leisure sectors, but we've also completed major engagements for household names in utilities, travel, media and retail. Our clients span the world: we've undertaken projects on every continent, and are comfortable working on-site when necessary.

"No job is too big, no job is too small." In our case, the cliché is true. We've advised banks on the strategic management of their payment card portfolios, we've helped start-ups write a business plan, we've built strategic alliances between leisure sector leaders, we've put sales forces on the road.

We have great respect for the numbers – data analysis and financial modelling are important tools for us – but we also believe in the power of creativity.

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