

CAUTION!

BANK TRANSFORMATION AHEAD

Welcome to the ‘New Normal.’ In this banking world of the future, the old business models are broken, and marketing takes on greater importance. The success formula includes stronger brands, more-engaged employees and compelling customer experiences.

BY MARY BETH SULLIVAN

WHAT IS THE U.S. FINANCIAL SERVICES INDUSTRY going to look like in the future? It’s difficult to say while so many challenges still exist. The clouds may have parted, but predicting how banking will take shape over the long term seems about as difficult as forecasting the weather a year from today. Given the current state of the economy, developments on the regulatory front, and the worsening mortgage foreclosure situation, we have a long way to go before the dust settles.

One thing is clear, however: The business models that drove growth and earnings in the past will not do so anymore. Companies hoping to succeed in the “new normal” will have to change their businesses in pretty dramatic ways. And if financial services companies change, that means that bank marketing will be transformed as well.



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We are, in fact, already beginning to witness changes to banking business models. The largest banks are heavily burdened by troubled real estate assets and are reducing investment in trading operations, refocusing on core businesses, simplifying their product lines and, in some cases,

shifting resources to global growth markets including China, Brazil and India.

Smaller community banks and thrifts with strong capital levels are looking for opportunities to boost small business and commercial and industrial lending to diversify their asset

The Future of Banking: Know Thy Customer, Know Thyself

Given the roller coaster ride of the past two years, it's hard to imagine anyone willing to claim they have a crystal ball capable of predicting the future of banking. But considering where we've been, there are a few certainties: Banking will never be the same (the federal government will make sure of that), and neither will customers.

Know thy customer

Just as consumers were forced to come to terms with their banking relationships over the past two years, banks are now forced to come to terms with their customers—or at least better knowing their customers. A bank's ability to understand who their customers are, not just what their bank accounts and products look like, will determine how successfully they attract and retain customers. Understanding who your customers are today—and who you'd like to have as customers tomorrow—will drive everything from product design and channel development to promotions and media selection.

When you take the time to really know your customers and what makes them right for your bank, it makes your organization and its offerings stronger. It makes your marketing smarter. It also requires discipline. You're forced to focus on strengthening and expanding existing relationships and attracting customers who are right for your bank rather than being all things to all people. Casting a wide net may seem attractive when looking at a large group of potential customers, but it's not the size of the net that matters today. It's the ability to cast the right net for the right customer.

Case in point: Regulation E changes to overdraft rules will force banks to seek revenue elsewhere. But where that revenue is generated isn't simply a math problem, but one that requires knowing customers well enough to be able to forecast the revenue potential of alternatives to overdraft programs *and* the impact to customer relationships. It's about identifying where product offerings, customer expectations and business requirements intersect.

And know thyself

After the crisis, we're seeing banks attempt to downplay their reality and play up what they think customers want to hear. The problem is, just because you say you're something, doesn't make it so. Customers can see past the campaigns touting good citizenship and friendly service to the reality of what they find when they enter a branch or call with a problem.

Have you built your brand on the idea that your bank is the friendly one? The one that goes above and beyond for customers? The one that takes their financial needs to heart? Then your solution to Regulation E certainly shouldn't fly in the face of the brand you've crafted by appearing punitive to the very customers you've been servicing (for example, a nonuse debit card fee).

You have the service of a small bank with the products of a big bank? You better make sure your product offering stacks up.

Or maybe your bank brand is built upon convenience. With lots of branches and expanded hours, that will certainly appeal to customers who expect to be able to have access to anywhere, anytime services. Does your Web banking platform reflect that ease of access? How about your mobile banking platform? Branch hours?

Today's customer is considerably more skeptical than yesterday's, and tomorrow's customer will be even more so. A long, hard look in the mirror may not be easy, but it's more important than ever.

The "right-sized" bank

Never before have regional and community banks had such an opportunity to capture business. From commercial accounts seeking a higher level of service to consumers who want transparency in their dealings with a financial institution, opportunity abounds. As a result of the crisis, whole movements sprung up to convince people to move their money to community banks in protest against "Wall Street." Small was good, big was bad.

But big isn't necessarily bad; just ask the business seeking a banking relationship capable of supporting its global expansion. Or a consumer who wants to know that she can find an ATM no matter where she's traveling—from New York to Nevada. Community banks, while meeting the financial needs of some customers, might not have the product breadth necessarily to meet the needs of others.

Today it isn't about size so much as it is about being right-sized—the right size to deliver the products, services that a customer wants and needs. And a customer's needs differ and change over time. Which is why knowing who you're servicing, and what they want from their bank has nothing to do with size and everything to do with being right-sized.

—Jennifer O'Connell, director, Financial Services,
PARTNERS+simons, Boston.

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bases away from mortgage and commercial real estate loans and also to focus on business lines where client satisfaction is largely driven by factors other than price. The forces of change are such today that *virtually all competitors must redefine themselves in order to survive.*

Let's make a quick review of the current economic and banking landscape and the various challenges facing financial services institutions. After this, I will summarize the implications of these challenges and describe the ways that bank marketing must evolve in order to keep abreast of changes.

Economy: big problems remain

The global economic situation remains uncertain—and this has important implications for all banking companies that rely on capital markets, interest rates and other factors now influenced greatly by global events. The mortgage foreclosure situation promises to delay significantly the cleanup of toxic assets and therefore delay the economic recovery. Consumers and small businesses—the engines of growth—lack confidence, which in turn, depresses spending and investment levels. We have been told we are experiencing a jobless recovery and a return to a slow-growth economy. If so, the economic engine that lifted so many before the crisis will not be seen again for a very long time.

Regulation: more coming

The regulatory burden has clearly increased, and with the buildout of the Consumer Financial Protection Board, the merging of the Office Thrift Supervision and the Office of Controller of the Currency, increased focus on anti-money laundering (AML), and other pending developments, we can expect to see more regulation, stricter enforcement and compliance costs. The risk exists for increased regulation to choke off innovation at precisely the time when financial services companies need new capabilities to drive new sources of revenue.

Consumer/business behavior: help me help myself

Early in the recession, as consumers and businesses began to save and pay down debt, economists were uncertain if this thrifter behavior would last. It has—and it's clear that it's here to stay. As a result, consumer and businesses are less interested in financial products and more interested in financial help. Trust is a major issue for many; surveys regularly indicate that consumers and businesses want help, but prefer the do-it-yourself (DIY) method, not trusting financial advisers to have their best interests at heart. That may change, but the

DIY mentality is spawning a plethora of personal financial management solutions, packaged small-business accounts with value defined around aiding cash flow management and the like.

Technology: The great 'disabler'

For many banks, technology remains the great "disabler." Core systems do not communicate with one another; accurate and timely customer information is elusive; technological improvement moves at snail's pace and delay necessary product, service and delivery improvements; and the level of technical expertise in-house is often weak. If technology is really to help competing companies become more efficient, more productive and more customer-centric, all of which are absolutely necessary for survival, we need to see substantially improved capabilities from the outsourced vendor community and technical expertise resident in-house to help drive change.

Successful banks will enjoy a higher percentage of profitable customer relationships, and many of these will be more highly profitable.

Implications

First, let's dispense with the more obvious implications of the recent crisis in the financial services industry: There will be fewer banks, probably far fewer 10 years from now. These reductions will be driven largely by a need to build capital through retained earnings, which will be tough to come by in a slow-growth economy that is not restoring lost jobs at a rapid pace. And, all of these needs will come at a time when the industry is burdened by higher regulatory costs. "Too big to fail" will be joined by "too small to succeed."

The community bank model will survive, and some community banks will prosper, but for those smaller banks that failed to invest in businesses other than mortgages or commercial real estate in the years leading up to the crisis, it will be very hard to transition to new strategies for earnings growth.

We may be on the verge of transformation at many banking companies. Successful banks in the future will exhibit five key characteristics:

1. Simplified core product sets coupled with more value propositions for targeted segments. We have already witnessed dramatic simplification of the checking product line at the nation's biggest banks. These simplified product lines provide far more clarity in terms of benefits for customers relative to the costs of the core banking account. The value proposition is moving away from products and towards other elements that will differentiate providers: ways to save toward predefined goals; connections to the community served by the bank; knowledge of

individual business sectors and how to help customers in these sectors manage their finances more effectively. These latter elements will become the basis for competing and for delivering value that customers will be willing to pay for.

2. **More distinctive brands.** With demand down for many banking products, it's critical to stand out from the competition. For too many years, banks have competed aggressively on the basis of price. Consumers and businesses, meanwhile, have increasingly rewarded companies that compete on other factors. The flight to quality we witnessed in banking has actually been happening on a much broader scale for many years.

Quality-based competition can take many forms: social responsibility, craftsmanship, innovation, ethics, engaging experiences, responsiveness—the list goes on. Banks are beginning to understand the importance of brand

and of being a distinct choice in a crowded marketplace. This year's most admired company for quality according to Fortune Magazine? Walt Disney. If you've been to a park, you know this company doesn't compete on price.

3. **Greater focus on fee-income businesses.** As interest rates rise and loan demand improves, many banks will enjoy expanding margins in their intermediation businesses—for a limited time. Over the long term, margins will continue to fall driven in part by intense competition for quality borrowers. Fee-income businesses will be critical for building revenues going forward. Banks that are unable to grow investment management, payments, insurance, processing, real estate management services, or add new fee-based services not even yet envisioned, will find it impossible to survive.
4. **More profitable customer relationships.** Successful banks will enjoy a *higher percentage* of profitable customer relationships, and many of these will be *more highly profitable*. First, however, banks need to do a much better job at analyzing and managing toward customer profitability. The majority of banks know very little about what drives profitability of individual customer relationships, and most fail to accurately reflect individual transaction behaviors, price sensitivities, risk profiles and other key factors into the profitability equation. When these factors are better understood, banks are well positioned to drive incremental business from individual customers—by pricing more effectively, targeting behaviors more specifically, and getting paid premiums for value-added services.

5. **Committed employees.** Banks that will succeed going forward must rely on their employees to make all of the above happen. Transforming the business models in banking today will not be easy; neither will getting people to do the hard work needed if they are not 100 percent committed to the objectives, understand their roles in the strategy, and are able to see change happen. Loyalty is earned; leadership, motivation, teamwork and communication must be engineered to drive loyalty. Loyal employees are the best marketers you have.

The role of marketing

The marketing function is absolutely *central* to delivering on the five characteristics of successful future banking companies. Banks that fail to view marketing as a strategic function will struggle to build their brands, engage their employees in the process, and create better customer experiences.

Successful banks will have far greater insight into individual customer behaviors and define ways to help customers to improve their financial lives and reach their financial goals. This requires more meaningful value propositions and better integration of business lines to deliver products and services more effectively. Building distinctive brands and improving the customer experience requires better customer intelligence put to use at the point of customer contact and better engineering of workflows across the value chain. Marketers must help to define the customer strategy, not just execute on it.

It may be time to reconsider the traditional bank marketing organizational structure. Most banks tend toward variations on a single design concept: product management, advertising and public relations, communications, market research, and other functional specialties form the basis for role definition. These functional specialties will need to give way to more customer-centric organizational definitions built around demonstrating superior knowledge of customers and the elements of the value chain that matter most.

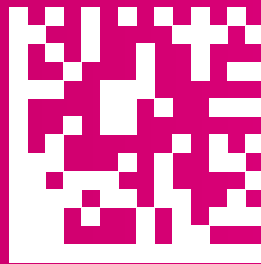
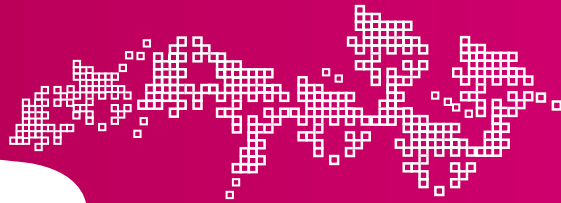
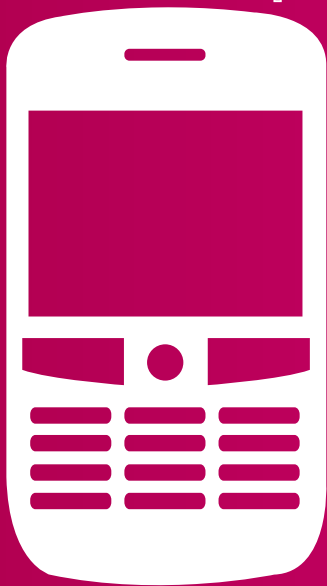
In a manufacturing operation, the traditional structure makes sense. But banking is moving toward an idea-based business model, no longer selling checking accounts and mortgages but rather delivering products and associated services that help individuals and business to live and perform better.

In the future, marketing will spend less time pushing things out and more time focused on individual customers—and the ties that bind them to the company. ■

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