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Introduction

BANK 2.0 was written at the start of a time of great disruption in the banking and financial services space. We were in the midst of a "global financial crisis", second only to the Great Depression for many commentators. In the midst of this chaos, however, the retail banking space faced an entirely different challenge as the cracks in the façade that was the "secure banking system" appeared.

> "Global Central banks have pumped $8.7tn into the banking system to 'save the world'. Saving the banks has cost more money than it cost to fight WWII, the first Gulf War, put a man on the moon, clean up after last year's Japanese Tsunami, and the entire African aid budget for the last 20 years all put together."
>
> —David McWilliams, PunkEconomics

This was not just a crisis of identity, a challenge to the perception of banks as "secure" and "socially responsible" bastions of the community. It was a challenge to the very role of banks in an open, transparent society. This was more than just the "occupy" movement and a backlash against unreasonable bonuses—bankers suddenly found themselves having to answer to the public for their decisions that led to the crisis.

Bankers rallied in this environment to claim how unjust negative public opinion was, how they had the right to make a profit (thanks for that gem, Brian Moynihan), how bankers needed to get huge bonuses because otherwise they might leave their employers, and that they were sick of the sledging they were getting from customers who really had no idea how banks or the banking system worked. Now you might think that's unfair, but those are the comments that stuck with customers in the midst of all this backlash.

The problem, however, was not one solely of perception, but of relevance. In an age where I use my mobile phone and the Internet more than I watch TV, and where bookstores, video rental stores and other mainstays of the physical retail commerce are quickly morphing, banks just appeared old-fashioned and out of touch.

In a world where I'm more likely to text you, update my status, upload a photo or use an app, rather than visit a bank branch—the change that was being thrust on bankers was not just a crisis of identity, forced transparency, and a battle for public opinion, but a crisis of modality. Retail banking was fundamentally ready to change the way it worked at the consumer interface, but the overwhelming tone of the industry was both a rejection of that notion and a dismissal of changing consumer needs at the same time. Bankers dismissed the concept that digital interactions were overtaking the branch, and reinforced the need for face-to-face interactions as superior when all they were really doing was trying to justify their bloated, costly, physical infrastructure.

It was in this environment that a new reality of banking started to emerge. Banking was no longer defined or hemmed in by a physical distribution network, or physical artefacts. The banking system emerging out of the global crisis would be one that was highly utilitarian, pervasive, mobile, and seamlessly engineered to work when and where we needed it. While the "death of cash" will still take many years to become a reality, the effects of the mobile phone and Internet are causing a massive shift in bank practices, distribution models and competitive landscape.

In the end, many of the banks that were household names during the 20th century will simply cease to exist as they are displaced or consolidated in the system-wide disruption that is soon coming. New players are emerging now that are taking ownership of the customer experience through revolutionary new techniques that attack the fringes of "banking" and payments.

PayPal, perhaps the largest financial institution in the world (by number of active customers), flourished by filling a gap in payments experience born out of a lukewarm industry reception to e-commerce, to become easily the dominant online payment provider. Now 12 years old, PayPal is still considered by many banks to be a "new" player in the sector, but for start-ups now disrupting the industry, PayPal is an incumbent.

Square, a company founded by Jack Dorsey of Twitter fame, went from start-up to a $4-billion business in revenue in just under two years, showing banks first that a point-of-sale terminal wasn't necessary, and then that even cards weren't necessary.

Simple (formerly BankSimple) emerged as one of the first non-bank entities that truly attacked the very front end of banking. Others quickly followed. The success of these start-ups is not yet certain, but with more than 100,000 registered customers when Simple opened its doors, so to speak, success would appear a simple matter of execution.

In the midst of all of this, a new class of consumer emerged in developed economies such as the US. This new class of consumer no longer needed a bank account to live and work in the system. In fact, millions of them abandoned their traditional bank relationships in favour of prepaid debit cards, PayPal accounts, mobile payments, and other such workarounds to a system that was coming apart at the seams. With $200 billion in prepaid debit cards in the US alone in 2011, this was not a minor blip, this signalled a fundamental change—the rise of the "de-banked".[1]

It has become clear that Bill Gates' quote of old about us needing banking, but not banks, has never been more likely an outcome of the technology and behavioural-led disruption we find ourselves in today.

In this revised edition, *Bank 3.0*, the message I want you to take away is this: Banking is no longer somewhere you go, it's something you do.

By this new measure, a customer's assessment of a service provider in the retail banking or financial services space will not be capital adequacy, branch network, products or rates. It will be how simply and easily customers can access banking when they need it, and how much they trust the partner or service provider to execute.

So if you're a bank—what are you going to do? How are you going to make the transition? When will you need to start scaling back branches? How real is this shift and how quickly will it happen?

While *Bank 3.0* retains some of the great case studies and groundwork that was in *Bank 2.0*, I've tried to update this based on the rapidly changing environment we've found ourselves in over the last few years. It's incredible how much has changed and what this means for the future of banking, and, as such, I felt these changes added tremendous value to the discussion. Much of the original content is gone, making way for a more relevant and up-to-date discussion.

For those of you who previously read *Bank 2.0*, this is an update that includes insight on the acceleration of mobile deployments, including detailed discussion on wallets and cardless solutions. We'll look at the differences between technologies such as NFC and Virtual Wallets, and what is the likely outcome for payments over the next decade, including how long before plastic cards are really on the decline. We'll look at what is happening in the web space as a result of our moving away from the PC browser to "screens", along with the death of Adobe Flash and the emergence of HTML 5. We're taking a much more detailed look at the implications of social media on your brand, how you engage customers and how this impacts organisation structure. We'll look into the emergence of journeys at the point of impact, and we'll look at the need for ever more pervasive banking solutions enabled through smart data and collaboration across disciplines and industries (e.g. mobile network operators and institutions.)

Be assured this is disruptive and controversial. This is about as exciting as banking gets. Everything from this point on is changing. What you used to consider as banking historically is about to get, not just a makeover, but a complete reboot.

If you're in retail banking, the future starts now and it's called BANK 3.0. Jump in, or get disrupted.

Endnotes

1 Ron Shevlin from Aité Group was the first to coin this word.

Part 01

Changes in Customer Behaviour

1 The Demands of the Hyperconnected Consumer

In 2011 the Internet surpassed television and newspapers as the primary news source for the Y-Gen demographic in the US.[1] In 2011 the average time spent daily using mobile phone apps surpassed the time people spent surfing the web on their PC.[2] In the US, approximately 25 per cent of all US households have no or very limited access to financial services,[3] while there is a 103 per cent adoption rate of mobile phones and a 76 per cent adoption of the Internet.[4] In Asia, there are 1.6 billion people without a basic bank account,[5] while in the same geography there are 2.6 billion mobile phones.[6]

In June 2011, the United Nations declared Internet access a basic human right.[7] By 2016 more than half the planet will own a smartphone with Internet access, and Internet access will basically come free with your monthly contract.[8] Today more people access the Internet via a mobile device than a PC. Tablets alone will pass PC sales in the next few years.[9]

We live in a world where being connected is not only a basic right, but an expectation, a simple foundation of our day-to-day lives. Today it's not enough to just be connected. Many of us live with multiple devices simultaneously. A smartphone or two, a tablet, a PC, a gaming device connected to the Internet, a web-enabled TV to stream content, and more. We live in a hyperconnected world.

My kids who are three, nine and twelve (at time of press) will never live in a world without a mobile phone or an Internet connection. They won't be able to conceptualise a world that never had "always on" messaging, social networks, multitouch tablets and other such technologies. They won't perceive of these technologies as unique, new, advanced or "alternative" channels. They'll simply expect the world to work in that context. If you don't—you're irrelevant.

With Facebook set to exceed one billion connected individuals in 2012,[10] it's likely that we'll soon have trouble finding even one of our friends who isn't on Facebook. Remember those holdouts who said they'd never ever use an ATM, have an email account, or use a mobile phone? There are those same responses to Facebook today, too. Now admittedly, Facebook might run out of steam (in terms of adoption) somewhere north of one billion users, but fewer than the estimated two billion users who already have an Internet connection—but that hardly makes Facebook a demonstrable failure, now, does it?

The fact is that the Internet, mobile apps, social media and other such innovations of the last 20 years are not special anymore. They might have been in 1999 to those of us who remember a time without them, but they are not new to anyone born after 2000. They just are part of the fabric of everyday life.

So when you are looking at your strategy for your bank and figuring out how quickly or holistically to integrate these technologies into your channel strategy, think about this. *This is the way banking will be done from this day forward, without exception. We're never going back to a world without internet banking access, mobile phones, social media and multitouch.* Thus, it just doesn't make sense to put off investment in these most basic of technologies that lay the foundation for the very future of banking. It's not like you can avoid the investment sometime in the future, or that you shouldn't take every opportunity to learn about them now, because they're absolutely critical for future revenue and engagement.

Now some might argue that it's not going to make that much of a difference delaying investment in digital. They'd be dead wrong. If the sceptics looked at every major industry that has been massively disrupted in recent times (books, music, newspapers, etc.), they would be certain to see that the businesses that believed in the status quo or didn't invest fast enough were the first casualties in the digital shift.

Clearly the expectation of the average consumer today is that you will simply provide access via this technology, just as you did via an ATM or a branch. You *have* to do this, you have no choice. As you'll see from this book, there's not even a choice of *when* you invest anymore—if you're not already heavily investing in all these technologies, you are well behind the behaviour and expectation curve, and you will be disrupted. In all likelihood, banks will be predominantly IT or technology companies in the near future, with banking simply the utility provided through that technology.

The average individual is spending 94 minutes or so a day using apps, checking emails and texting up to 100 times per day.[11] We're logging on to mobile banking 20–30 times per month[12] and internet banking around 7–10 times per month,[13] but visiting a branch only a few times a year.[14] We're shopping online and via mobile with increasing voracity, and we're even using our phone in-store to check prices of comparative goods we see on the shelf with others available online or around the corner. Amazon has even used this behavioural strategy specifically against the likes of Best Buy in the US. These are not novel experiences for the average consumer anymore, they are just the way we live our lives in the 21st century.

Being "always on" or hyperconnected presents its own challenges. Many users of such pervasive technologies are finding it increasingly difficult to detach themselves from such "always on" access and service, either because of demands from their employers/clients for uninterrupted access, or worse, because of addictions to connectivity. This almost compulsive need to stay connected is just one of the side effects of the Information Age.[15]

The customers of the Information Age have been empowered by greater choice, greater access, and better, faster, more efficient modes of delivery and service. To understand why resistance to technology investment is futile, we must recognise the underlying forces at work.

There are two major factors creating behavioural change, namely the ***psychological impact*** of the Information Age and the associated innovations, and the ***process of diffusion*** (of innovations). Each of these factors contributes to create a paradigm shift in the way financial institutions need to think about service and engagement of customers. There are ***four phases of disruption*** that constitute this behavioural paradigm shift with respect to consumers. These have serious long-term implications for banks and financial institutions.

Psychological impact

To understand the core psychological drivers at work in the modern, hyperconnected consumer, we need to revisit one of the foundational pieces of work in respect of the theory of motivation—that of Maslow's hierarchy of needs.[16] Abraham Maslow studied exemplary people of his era such as Albert Einstein, Jane Addams, Eleanor Roosevelt, and Frederick Douglass, and determined the hierarchical progression of the individual—essentially what amounts to a theory of positive motivation and personal development.

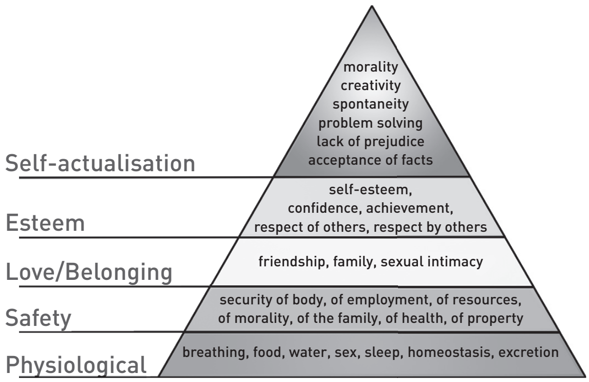

Figure 1.1: Maslow's hierarchy of needs (c. 1943)
(Credit: Wikipedia Creative Commons)

The growth of technology and more efficient service paths and ways to meet our self-actualisation needs have shifted the way we value our time, set expectations and perceive ourselves in our environment. For example, we understand through the introduction of new communications channels that if we can do something via phone or online, we are essentially wasting our time by persisting with a traditional interaction that is far less time-efficient. This, in turn, increases our self-esteem because we are using our time more wisely. Secondly, the execution of a transaction or a purchase *without* the assistance of a person, as long as it works well, gives us a feeling of control and self-achievement that cannot be achieved in a traditional interaction. Let me illustrate…

Take a mortgage proposition from the 1970s in middle America. Let's say I wanted to purchase a family home, but needed a mortgage from the bank to accomplish that. In those days, I would need to drive down to the local bank, make an appointment with the manager, and then prepare myself for an intense grovelling session to see if I could possibly convince the bank manager to give me his approval. If the bank manager liked me, or knew my family, or my business was strategic to the bank, then I might get an offer, but I had zero control of rates, fees and such, as the bank was totally in control. This might have led me as a customer to feel helpless, especially if the application was rejected.

Banks at the time began to believe it was ok to reject their customers and effectively started saying to them: "If you're lucky, if we approve your application, we might just let you be our customer." These days, the customer has much greater control over this type of interaction and is not dependent on a limited set of providers, and so he is empowered.

In 2008 the biggest seller of home loans in the United States was Countrywide, acquired by Bank of America in 2009 for US$4.1 billion in stock. Now before you start with the fact that the Department of Justice went after Countrywide, and they had massive losses associated with subprime, remember that none of this has anything at all to do with the fact that Countrywide proved repeatedly that you could sell a complex mortgage product online, that you didn't need a face-to-face interaction. I hear time and again from supporters of the branch that you need branches to sell mortgages, but that is simply not correct. Countrywide had more than nine million home mortgages on its books which originated online[17] at the time of the sale.

This is not specific behaviour for a younger demographic of first home buyers either. Generation X (born 1964–75) and baby boomers (born 1946–63) are the most likely candidates to research mortgages online.[18] Savings from online mortgage offerings also abound.[19] MyRate, a successful Australian online mortgage provider backed by ING, claims it can save borrowers about A$80,000 on a A$300,000, 30-year loan because of the savings the online channel produces. Mortgagebot reported in 2010 that 88 per cent of people who completed online mortgage applications were between 19 and 59 years of age.[20]

Google Finance Australia reported that 88 per cent of Internet users in Australia start their search looking for a mortgage online, and spend between six and 11 hours researching the mortgage before they select a potential provider and reach out to them.[21] When they do contact a mortgage provider, increasingly it will be via the website, rather than by walking into a branch or phoning the call centre. In the UK and the US results parallel this behaviourally. The myth that customers require a branch to buy a mortgage is just that, a myth. It is more than likely that the majority of mortgages sold today were actually selected by the customer online, and the branch was just a step in the application process.

Rather than feel threatened by this, traditional lenders should be buoyed by the fact that one of their most profitable products is so easily enabled through low-cost, digital channels. In fact, in the US alone, close to 50 per cent of lenders take 25 per cent or more of their mortgage applications online, and 61 per cent of all the loans that were submitted through third-party underwriting engines were approved online, according to the Mortgagebot study mentioned earlier. This is simply mainstream behaviour now. It's not new, it's not emerging—it's how the mass market behaves.

So let's get back to the psychological influences that these technology and competitive choices give me as an individual. **I am in control** and if the mortgage provider's offer doesn't meet my expectations—I walk away. I have an abundance of choices, and **I am better informed** because of access to extensive informational resources. **I get better deals** because service providers have to work harder to get my business, and **I save money** because the margins have been squeezed through better delivery methods and more competition. **I get a better-quality solution** because mortgage products fit my needs much more precisely than the one-size-fits-all solutions that I was restricted to previously.

How do I feel about this environment as a consumer, compared with the consumer of the 1970s example? In terms of Maslow's hierarchy, I associate these positive changes as personal development and an improvement in the perception of self. I am more motivated and feel better about myself, I am happier and **in control**.

Over time my overall expectations of my service providers in the finance sector have been lifted to where I now *expect* an element of self-control, efficiency and choice that I didn't have available to me previously. This then moves from being a nice *change of pace* to becoming a *driver of choice and selection*, and I penalise providers who aren't able to offer me this flexibility and level of control/empowerment.

Process of diffusion

We'll talk more about this in later chapters, but the other key factor in the shifting behaviour of customers is the increasing acceptance of technology and innovation in our daily lives. At the start of the 20th century, several fundamental new technologies were coming or had recently emerged onto the scene, namely the automobile (1886), electricity (1873), radio (1906), the telephone, and, in 1903, the aeroplane. This was the dawn of a new age in industrialisation and innovation that caused leaders of the world to claim these improvements would usher in a new age of peace and prosperity. However, we do share in common with our brothers of the 19th century the inevitable sceptics who could not envisage a world that was changing as a result of technological improvement:

> "Lee DeForest has said in many newspapers and over his signature that it would be possible to transmit the human voice across the Atlantic before many years. Based on these absurd and deliberately misleading statements, the misguided public … has been persuaded to purchase stock in his company…"
>
> — A US District Attorney, prosecuting DeForest for selling stock fraudulently via US Mail for his Radio Telephone Company in 1913

New technologies that emerged in one geography took a lot longer to cross the seas in those days. Mass production was only just starting at the turn of the 20th century so getting products out of the factory and into the hands of distributors was a lot more difficult. There were not the large, mass retail brands and businesses that we have today; retail was often limited to the independently owned corner store or high street location. All these factors limited distribution and mass adoption.

By the late 1960s, Moore's Law had kicked into gear, and miniaturisation and the "'tronics" fad were leading to an increasing appetite for new gadgets and devices. In the late 60s, TV commercials and print advertisements often touted a science fiction-like future for consumers that was just decades away. Technology and innovation were capturing the imagination of society.

"I think there is a world market for maybe five computers." *Thomas Watson, IBM Chairman, 1943*

In 1975 IBM invented the personal computer. It wouldn't be launched until a few years later, but it just showed how far technology had come in the three decades since 1943 when the chairman of IBM had envisaged that there would be a total market globally for only five computers.

Introduced in 1977, the Apple II[22] became one of the most successful mass-produced microcomputer products of all time, based on market share. The Apple II line continued to be sold until 1993.

Within 10 years of the launch of the IBM PC and the Apple II, terms such as DOS, mouse, keyboard, disk drive and dot matrix were in the common vernacular. By 1995, when Microsoft launched Windows 95, the desktop computer was already a global phenomenon accessible to more than 90 per cent of the world's population and with adoption rates of more than 25 per cent in most of the developed economies of the world. The launch of the cellphone in 1983 by Motorola set the pace at which consumers were being bombarded with new and revolutionary technologies.

Then in 1991 the Internet burst onto the world scene. The web was commercialised by 1994 and reached the dizzy heights of the dot-com bubble in 1999. I say dizzy heights, but the fact is that Internet adoption actually accelerated after the dot-com period, and did not slow down until around 2006 in most developed economies. History bears witness that the dot-com bubble collapse was not a collapse in Internet or technology adoption by any measure.

The rate of diffusion is the speed at which a new idea spreads from one consumer to the next. Adoption is similar to diffusion except that it also deals with the psychological processes an individual goes through, rather than an aggregate market process. What has been steadily happening

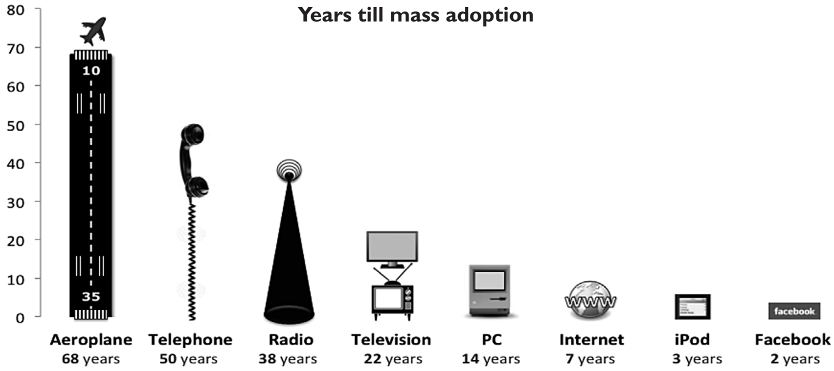

Figure 1.2: Technology adoption rates over the last 100 years

since the late 1800s is that the rates of technology adoption and diffusion into society have both been getting faster. While the telephone took approximately 50 years to reach critical mass,[23] television took just half that (around 22–25 years), mobile or cellular phones and PCs about 12–14 years (half again), and then the Internet took just seven years (half again).

Ultimately new technologies and initiatives such as the iPod and Facebook are now being adopted by consumers *en masse* in a period measuring months, not years. To illustrate this shift, Apple sold more iOS devices in 2011 alone than all the Macs it had ever sold in the 28 years prior.

> *"This 55m [iPads sold to-date] is something no one would have guessed. Including us. To put it in context, it took us 22 years to sell 55 million Macs. It took us about 5 years to sell 22 million iPods, and it took us about 3 years to sell that many iPhones. And so, this thing is, as you said, it's on a trajectory that's off the charts…"*
>
> —Tim Cook, Apple CEO during February 2012 reporting call

Apple then sold more iPhone 4S devices in fiscal Q1 of 2012 than in the preceding 12 months.

As we become more used to technology and innovation, it is taking us less time to adopt these technologies in our lives, and this further encourages innovation and thus increases the impact on business (which has less time to adapt).

Simply put: If you aren't introducing innovations into the customer experience at the same rate at which customers are adopting these new technologies, you are at a considerable disadvantage and risk losing your customers as more agile intermediaries and third parties capture the benefit of the innovation. Justifying your slow innovation because you are "the Bank", "we're a heavily regulated industry", or your legacy system/processes won't allow it just doesn't cut it anymore.

The core problem is that consumer behaviour is shifting with technology at the centre of that shift, but largely the "bank" is staying the same in respect of behaviour around onboarding, application processes and channel biases. This creates a significant behavioural gap between the consumer and the institution—one that is now being filled rapidly by better-positioned non-bank competitors like PayPal, Square, Apple, Starbucks, P2P lenders and many more.

For those of you who are thinking your organisation needs to watch for ROI (Return on Investment) to be demonstrated first or that maybe you'll be a fast follower, think of this. If it takes just months now for new emergent technologies to insert themselves into the mainstream and change behaviour, and if you've got a 12–24 month development and deployment cycle (typical of most banks' IT departments)—you'll be at least three to four years behind if you wait to see someone else's ROI demonstrated before you commit. Three to four years is the time it took Facebook to go from nowhere to half a billion users.

Here's how Jeff Bezos puts it:

> "I am emphasizing the self-service nature of these platforms because it's important for a reason I think is somewhat non-obvious: even well-meaning gatekeepers slow innovation. When a platform is self-service, even the improbable ideas can get tried, because there's no expert gatekeeper ready to say "that will never work!" And guess what—many of those improbable ideas do work, and society is the beneficiary of that diversity."
>
> —Amazon Form 8-K filing,
> Amazon.com Inc, 13 April 2012

You could be dead in three years with a fast-follower approach. That's more than enough time for a disruptive business to take a big chunk of your customers, for your revenue to disappear, or for the remaining margin you have to be hammered into non-existence.

If you're not constantly adapting and moving, you may as well just resign now, because you're already a dinosaur, and someone is trying to disrupt your ar… architecture?

The four phases of behavioural disruption

There are four stages or phases to the disruption occurring within retail financial services and each stage is disruptive enough to be a "game changer". However, by the time the third phase impacts retail banking, the changes will be complete and irreversible, resulting in a fracturing of the commercial banking business as we know it today.

The *first phase* occurred with the **arrival of the Internet**, and was amplified by social media. While many banks denied it at the time of the dot-com bubble, the Internet changed forever the way customers accessed their bank and their money. As we discussed in the psychology of customer behaviour, this gave them *control* and *choice* that were not available previously. Suddenly, customers were thrust into an environment where they could access their money as they wished, when they wished. As internet banking capability improved, the drive to visit the branch started to diminish, and customers began to rely on the new channel as their *primary* access point with the bank for day-to-day transactions. Within just 10 short years, we've gone from 50–60 per cent of transactions done over the counter at the branch to 95 per cent of our day-to-day transactions now going through the mobile, Internet, call centre and ATM.[24] Game changing…

In the later part of this first phase, in parallel to the start of the second phase, was the emergence of social media. Social media is a sort of theme running contiguously throughout each of the four phases, but it was enabled by the Internet (obviously). The key to understanding the disruption of social media can be seen not only in base crusades such as the Occupy Movement, but in the fundamental shift in power within the customer value exchange (see Chapter 5).

In retail banking previously, banks had the enviable position of being able to "reject" customers because they were too risky, or not profitable enough. Customers would come to the bank, jump through all these hoops called "KYC" (Know-Your-Customer), and if the bank didn't like them, sorry—they didn't qualify. Some of my banker friends refer to this as the "lucky to be a customer" philosophy. Banks got complacent enough to think that they could summarily reject customers on the basis of risk because that would lead to better profitability. This, of course, flies in the face of the perceived role of banks in society, where they are seen to provide a basic social right. In turn, over time this has led to a very cynical view by the public of the inequality of the bank-customer relationship.

The flip side of this in the social media age is that today, customers are assessing bank brands with a social lens that now lets them reject stupid bank policies, or the entire brand, based on recommendations from the "crowd". Essentially, the power of my friends and network is such that if the crowd tells me your bank sucks, there is no amount of advertising spend you can leverage that will bring me back to your brand. In the age of social media, the balance of "value" has tipped back in favour of the consumer, and has weakened the value proposition of the average bank brand.

No longer do banks have the luxury of being able to deal with customers unilaterally and without respect for the crowd, as Bank of America recently found out when it raised basic checking account fees as a result of the Durbin Amendment. It took just weeks of public pressure via social media to push them to reverse this decision. Trust is no longer a given in the social exposed world. I'll trust your brand when you engage with me openly and honestly, with a real commitment to service.

The *second phase* is occurring right now. The emergence of the **smart device** or **app phone,** such as the iPhone and Google Android-enabled phone, is a driver for portable or mobile banking. This has extended into the world of tablets and generic device "screens" that enable web or app access. While there's debate over the security and ROI (Return on Investment) of these screens, customers don't make that distinction—they just adopt. Already many banks are deploying what amounts to a cashless

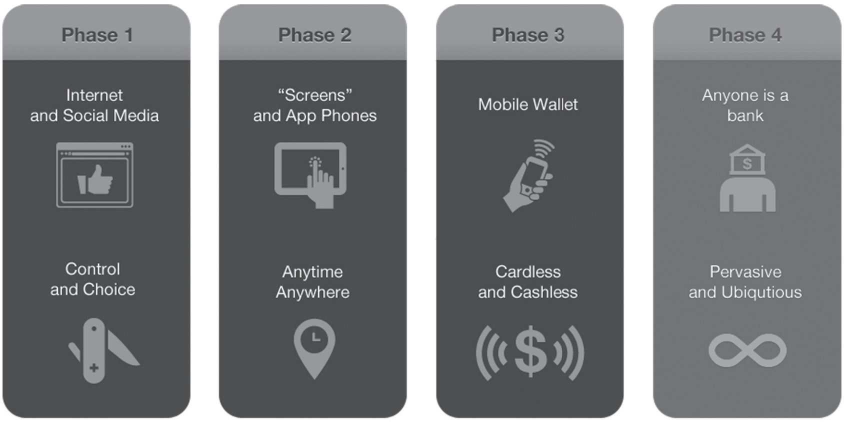

Figure 1.3: Four phases of behavioural disruption (Illustration: Sebastian Gard)

ATM on a mobile application platform—yes, you can do everything on a mobile phone that you can do on an ATM, *except* withdraw or deposit cash. You can even deposit cheques via remote deposit capture technology.

Here are a few statistics that support the second-phase disruptive model:

- The US has a more than 100 per cent adoption rate of mobile phones (some people have more than one), and one-third of households are mobile-only now.[25]
- China has more than 950 million mobile users, almost three times that of the US,[26] and the number is growing at the rate of 20 per cent annually over the last decade. It has over 500 million Internet users—that's twice what the US has.
- China Mobile is deploying one million WiFi hot spots around China for ad-supported, free wireless access.
- The US population sends over two trillion text messages annually. It's estimated that more than 15 billion text messages were sent in China in just the first two days of Chinese New Year, contributing to the three trillion text messages expected in 2012.
- As of December 2011, smartphone users spend on average 94 minutes a day using apps, compared with 72 minutes using the web on browsers.[27]

- 99 per cent of mobile banking users view balances, 90 per cent view transaction details; about $10 billion of funds have been moved via mobile transfers/bill pay; 15 million location-based searches are being performed (annual run rate).
- More than 50 per cent of iPhone users have used mobile banking in the past 30 days, according to Javelin Strategy; 32 million Americans access mobile banking on their smartphone as of June 2011—a 45 per cent increase since 2010.
- 33 per cent of mobile banking users monitor accounts daily, 80 per cent weekly, also according to Javelin Strategy.

So if we didn't need physical cash or a plastic card, what would happen then? This is the *third phase*—when we move to **mobile payments** on a broad scale. NFC-based (Near-Field Contactless) mobile wallets and stored value card micropayments are already here, but more is to come. The third phase also involves the convergence of our mobile phone and our credit/debit card, which is a logical technical step in the next five years. When these changes occur, our need for cash will reduce rapidly, and the disruption will be far-reaching.

In the UK 43 per cent of payments is done by debit card, and 23 per cent by credit card.[28] Cash still makes up 32 per cent of retail payments, but as a percentage of the whole, it is expected to reduce by a further 20 per cent over the next five years. Cheques make up just over two per cent of payments these days, so it is not hard to see these disappear entirely in the UK within three to five years. As the growth of debit cards swells further and other mobile payments such person-to-person (P2P) are enabled on our phones, this will further reduce legacy payment methods.

It is not unimaginable to see 85–90 per cent of UK retail payments done by mobile/card in the next five years. In markets such as Japan, Korea, and Hong Kong, the requirement for cash may be even less compared with mobile payments.

While cash is not going to disappear overnight like cheques are, the fact is that mobile payments will accelerate the already declining use of hard currency. Between 2007 and 2010 in Australia, cash as a payment method at the retail point of sale declined from 40 per cent to 30 per cent,[29] the fastest decline in cash use we've ever seen anywhere. US consumers' use of cash is predicted to decline by 17 per cent between 2010 and 2015.[30] In the UK, cash was seen in 73 per cent of retail transactions in 2000, but will be a fraction of that by 2018.[31]

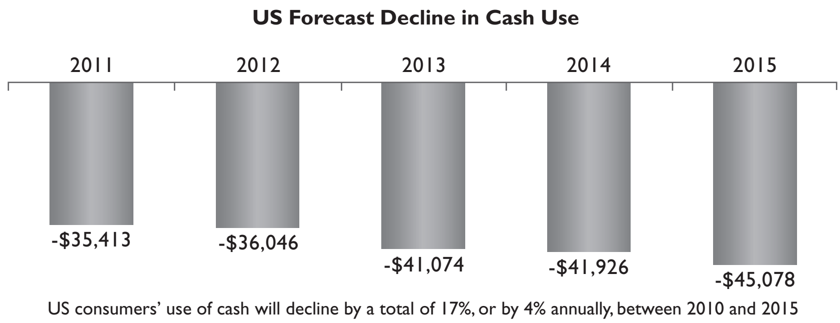

Figure 1.4: Decline in Cash Use—US Forecast (Source: Aité Group)

There are the great unbanked who don't yet have a bank account and who currently rely heavily on cash and prepaid debit cards, but as we will see with M-Pesa and G-Cash (Chapter 6), this is hardly a hurdle for mobile cash and payments. The success of the Octopus card in Hong Kong, T-money in Korea, Edy and Suica in Japan, and other emerging technologies already prove the concept. What would quickly kill the need for cash in its entirety is a technical standard for mobile money that could be adopted globally by network operators and device manufacturers.

Even if only 50 per cent of cash transactions are replaced by electronic stored value cards, debit cards and mobile wallets in the next five to ten years, the current ATM and branch infrastructure that supports cash becomes untenable from a cost-burden perspective. If we no longer need to go to the ATM to withdraw physical cash or currency, then pretty much everything we do on the ATM today can be done on our mobile app phones. If branches no longer need to deal with cash, then a large part of the reason for their existence disappears.

In 2000, 59.5 per cent of retail payments in the United States were made via cheque. **That number plummeted to just 4.3 per cent in 2010.**[32] In Australia this decline has been even more severe. In 1995, 80 per cent of non-cash retail payments were made by cheque. **That number was just 3.3 per cent in 2010.**[33] In 1990, 11 million cheques a day were written in Britain. This number ballooned to 36 million cheques a day by 2003. According to the UK Payments Council report mentioned earlier**, fewer than one million cheques per day** will pass through the system in the UK **in 2012**, but more significantly, **by 2018 cheques will make up less than 0.8 per cent of personal payments.**[34] Regardless of UK Payments Council edicts, this translates to the death of cheques in short order.

Traditionalists might argue that the value of cheques still in the system is high, and thus more likely a part of business transactions and other such payments that are unlikely to shift to cards or other mechanisms in the near term. To balance out this claim, bear in mind this simple and undeniable fact. There is not a single economy or banking system in the world today where cheque usage is trending against a decline—not one. There is no use talking about saving cheques—these antiquated artefacts are in their death throes. The mobile wallet and person-to-person payments will simply accelerate the demise.

As we'll see in Chapter 12, every man and his dog wants a part of the mobile wallet—from Google, PayPal, mobile operators, handset manufacturers, mobile OS creators, app developers, start-ups, and banks. Phase Three is not just about the death of cheques and cash, it is about the loss of physicality. It is where we no longer need physical interactions with a bank for basic, day-to-day banking.

So what happens when Phase Three hits? From that point on the battle for the basic bank account will be on. The likely outcome is that for the great unbanked (approximately 61–64 per cent of the planet[35]), the phone will become the day-to-day bank account of the near future. While the average banker might dismiss this as immaterial to his traditional business, the unhinging of the bank account from the bank spells massive disruption for the financial services industry. It means that eventually the bank account will just be a value store commodity. While some form of e-money licensing, such as that in the UK, is likely to regulate and protect consumers, the taking of a deposit will no longer require a full banking licence.

Think of this. What's the difference between a balance on an Oyster, Octopus or a prepaid MetroCard, and a deposit in a CASA (Checking Account/Savings Account) account? How would we explain the difference in deposit taking mechanisms for a basic bank account, prepaid debit card and a prepaid telephone contract? What if our prepaid telephone account allowed us to pay at a point of sale using an NFC-enabled phone?

This is where the *fourth phase* emerges. If you think a banking licence restricts everyone except banks from taking deposits, you just haven't been paying very much attention, have you? When banks lose the basic day-to-day bank account to the mobile phone or commodity value store, the rest of banking is down to specialist banking products, investment management, and the movement of funds.

Phase Four is about banking no longer being somewhere we go, but something we just do. It is the realisation that the best way to deliver banking products and services is *pervasively*, wherever and whenever a customer needs the utility of a bank. The fact that banks simply don't have the ubiquitous coverage to deliver these products and services in the new world, and that a whole slew of partnerships will be required to ensure the product or service gets to the customer at the point he needs that banking utility will be a revelation to many. This is where retail distribution becomes unhinged from product manufacturing and risk mitigation. It's a time when you won't need to be a bank at all to provide what we've traditionally called banking, and it's already happening.

Customers will go about their daily lives with banking embedded into processes that require financial products or transactional support. The home-buying experience will integrate the mortgage sale, and we won't need to see a mortgage officer. Travel websites will not only integrate products such as travel insurance but will allow us to take a loan for our trip instead of using a debit card or credit card to pay for the flight. A car dealer sells us a leasing deal for that new car we bought. A retailer gives us a line of credit for that furniture we bought using our mobile wallet. Someone else owns the customer, banks become the manufacturers, networks and processes that support the utility of banking.

Phase Four will produce a fundamental split between banking as a distribution business and banking as a product-manufacturing or creditprovisioning capability, with banking never to be the same again. Banks can either own the product, transaction and payment platforms, integrate the technology, and embrace broad partnerships OR protest with their last dying gasp of breath that things are not really going to change. "The branch is back", "Cash is king", "Cheques will bounce back"—yeah, ok, and let's bring back vinyl records, telexes, VCRs and cassette tapes while we're at it!

Retail banking disruption and the de-banked

These changes, both with regard to psychology and consumer adoption cycles, have empowered and liberated customers, but represent a real threat to the industry. As Evans and Wurster first posited in their book, *Blown to Bits* (2000)**,** the threat for traditional intermediaries is that their business faces potential deconstruction if they cannot encapsulate their place in the value chain in new ways by utilising technology and innovation. This is increasingly why traditional intermediaries such as travel agents and stockbrokers are facing an impossible task of maintaining margins and restricting churn[36] or loss.

Online stock trading, first embraced by Charles Schwab and the likes of E*Trade, was phenomenally successful in the early days of the commercial World Wide Web, and still is. But there was significant resistance from the likes of traditional players such as Merrill Lynch, which regarded e-trading as a threat to its traditional brokerage model.

The difference in approach between the Charles Schwabs of the world and the Merrills of the world is perhaps the essence in identifying how an organisation copes with challenges presented by innovative technologies in the customer experience.

> "The do-it-yourself model of investing, centered on Internet trading, should be regarded as a serious threat to Americans' financial lives."
>
> —John "Launny" Steffens,
> Merrill Lynch vice-chairman, September 1998[37]

One reaction is to resist the change because it is uncomfortable and potentially "breaks" your traditional view of the world, while the alternative reaction is to realise that this is simply the inevitability of momentum and you need to figure out how to capitaliseon it, or benefit from it. Occasionally such new technologies turn out to be failures (not fads), like 8-Track, BETA video and WAP. This is due to the fact that, more often than not, the new technology is surpassed by something better. The lessons we learn in the first generation of the technology, however, are typically invaluable for future applications.

Today the Korean Stock Exchange owes 90 per cent[38] of its volume to internet trades, NASDAQ sees more than 60 per cent of its daily trading volume come from ECN (Electronic Communications Networks), and regional exchanges such as the CME (Chicago Mercantile Exchange) achieve more than 80 per cent of their volume from electronic trades. Between 2006 and 2007 the New York Mercantile Exchange observed an increase in electronic trading volume of 86 per cent,[39] leading to an overall increase in trading volume of 38 per cent. Today that figure is well above 70 per cent. It would appear by any measure that the online trading experience has been successful.

In Hong Kong, HSBC launched its online trading platform in 2001. Today, more than one million trades each month are completed on that platform. If this facility were to be shut down, there is no way the traditional channels of HSBC could cope with even half of this volume of transactions. Meanwhile, the more than 280 brokerage firms that were present in Hong Kong during the late 90s have dwindled to fewer than 80 players.[40] Indeed, internet trading was a *serious threat*—but not to consumers, only to traditional brokerage firms that weren't ready to adapt.

The more advantageous of these transformations have empowered customers in ways that a 1950s bank manager could only have had nightmares about. To illustrate, below is a list of retail banking products and the average approval times for applications, comparing 1980 and 2008.

Table 1.1: Comparison of Product Application Approval Times

Product	1980	2008
Credit Card	14 days	Instant approval
Personal Loan	7–14 days	Pre-approved, or 24 hours
Home Mortgage	30 days+	24 hours[41]

These product application approval times are indicative of the pressure on financial service providers to adapt to the changing expectations of customers, and the need to stay competitive. Barriers to entry are lowering, and new innovations in business models are creating pseudo banking services streamed right to our desktop, supermarket or corner 7-Eleven store.

Here's how I articulated this disruption for bankers in my last book, *Branch Today, Gone Tomorrow*:

> "Everything about retail financial services that relies on outmoded physical artefacts, proprietary and outdated networks, and processes that are complex and unwieldy—all lend themselves to disruption. If you can think of a better way to do your banking, then you already realize that the current status quo is not sustainable. In today's environment, if you can imagine it, then someone is probably building it.
>
> "If you are an incumbent player you might argue, for example, that NFC requires critical mass to reach adoption, but so did the Internet, so did music downloads, so did Wikipedia and electronic stock trading. The question is, do you wait until the disruption takes place to start planning for the new reality?"

The new value is not being a "bank". The new value is understanding the context banking products and services play in the life of the consumer, and delivering those products and services on that basis. The customer will expect and demand this type of integration. He will have no patience for a bank that insists he comes to its "place" before he can have access to banking.

There are two big threats to retail financial services distribution strategies today. The first is simply changing behaviour with respect to where and how the consumer shops for financial service products. The second is the proliferation of alternatives to traditional financial service organisations.

There's a growing group of consumers in the United States who have no checking/current or savings account, and they number in the tens of millions.[42] This group of unbanked or underbanked is increasing in size instead of decreasing, as conventional wisdom would dictate. Ron Shevlin from Aité Research Group aptly coined the word "de-banked" to describe the behaviour of this growing group of hyperconnected consumers who are abandoning traditional banking relationships. So how can they survive without a bank account?

This is where the fastest growing form of payments in the US comes into play today, namely prepaid debit cards. As an industry, this business has grown from $2.7 billion in 2005 to $202 billion in 2012. In November 2011, the Center for Financial Services Innovation (CFSI) released new data about the 2010 underbanked market. The research found that:

- Underbanked consumers in the US generated approximately $45 billion in fee and interest revenue for financial services providers in 2010.
- The total dollar volume of the underbanked marketplace in 2010 was approximately $455 billion in principal borrowed, dollars transacted, and deposits held.
- The market has shown strong growth in certain segments: payment services grew by six per cent from 2009 to 2010; credit services grew by two per cent in the same period.
- Approximately half of this group have college education, and close to 25 per cent of the underbanked segment are prime credit rated.

Several individual products witnessed very high revenue growth rates between 2009 and 2010: Internet-based payday lending (35 per cent), general purpose reloadable (GPR) prepaid cards (33 per cent), and payroll cards (25 per cent).

This appears to be a global phenomenon too. In China the prepaid debit card market came very close to $250 billion in 2011, and is growing at close to 30 per cent per year. Programme managers of prepaid debit cards can be any organisation—supermarket chains, private companies, telecoms companies, retailers, sporting clubs and memberships. There's a whole lot of non-bank organisations providing basic bank accounts today.

Niche payment solutions such as iTunes and other loyalty cards are also becoming increasingly commonplace for day-to-day transactions. *The Wall Street Journal* reports that the Starbucks Card sees more transaction volume than any in-store loyalty card of its kind.[43] A total of $2.2 billion was loaded onto Starbucks Cards in the year through to September 2011, up 151 per cent from the same period of 2006. Reportedly 25 per cent of in-store purchases at Starbucks are now made via their Starbucks Card Mobile App, accounting for 27 per cent of US domestic retail revenue.[44]

The bank account is becoming unhinged from the bank. Mobile is the ultimate disruptor in this shift. Once we can pay with our phone, and it is connected to a value store—this is a far better banking utility than a basic current/checking account. A bank still issuing cheque books simply doesn't provide a competitive platform to compete with a mobile wallet, and as we've already seen, businesses don't need a banking licence to power a value store on a wallet.

So how does this affect the future of banking? As value stores begin to abound and the mobile wallet gets hooked into everything from the iTunes store to Facebook credits, to loyalty cards, transport systems, and beyond, the basic bank account becomes impossible to differentiate, and will be the ultimate commodity. In the UK and markets such as Hong Kong, the regulators have responded to this increasing pressure by creating a sort of subsidiary banking structure for "e-money" or, in the case of Hong Kong, for basic deposit taking.

The problem for banks is that the ability to store a balance or take deposits is no longer the sole domain of "banks" that have a full-blown banking licence. The cost of this is significant. In 2011 almost $40 billion in deposits was freed from traditional banks to credit unions and the like, along with an additional $200 billion in prepaid cards, resulting in the loss of approximately $12 billion in revenue (including overdraft fees, monthly fees, lending fees, and interchange) for the incumbents. Again, look to de-banked consumers as an emerging group effecting this change.

The problem for banks is that increasingly this group of de-banked customers who use non-bank value stores for power purchasing are not the poor underprivileged struggling with unemployment and with dismal credit ratings (as banks imagine they might be). Increasingly these are technology-enabled professionals, university graduates with prime credit ratings. Valuable future customers for sure, but hardly unattractive today either.

You might argue that the most profitable high-net-worth customers or mortgage holders are hardly going to unhinge themselves entirely from the banking system. You'd be correct. But the problem with the unhinging of the bank account is not that you'll lose the high-end, investment-class business. The problem is that you lose the day-to-day connection with the customer.

The key to really understanding the fourth phase of disruption is that we all need the utility of banking, but increasingly we don't need a bank to provide that utility. Understanding that utility is the core value of a banked relationship, and not the "bank" itself, is a harsh realisation that most bankers will not be able to deal with philosophically. Those bankers are the targets for disruptors, as the bookstore was for Amazon.

The disruption that is occurring in the customer experience is all about removing friction in outmoded or outdated processes for customers. Whenever you tell a customer he needs to fill out manual paperwork, or visit a physical location, you're increasingly going to get kickback from a growing segment of the market. While many will argue passionately for the role of a face-to-face interaction and the "richness" of the branch experience, the reality is that there are two reasons most customers will baulk at that.

Firstly, they don't have the time or they perceive it is faster to go an alternative route—convenience was always a key driver for disruptors such as Amazon and iTunes. Secondly, we're being trained that we can open pretty much any non-bank relationship completely digitally today—so KYC (Know-Your-Customer) issues aside, the push is for rapid, digital onboarding of customers. In usability terms we call the latter a design pattern and it ends up driving consumer's expectations because it is an entrenched behavioural expectation.

Digital natives won't be able to figure out why they can sign up for Facebook, iTunes, PayPal and other relationships completely electronically, but your bank still requires a signature. It defies logic for the modern consumer, and no amount of arguing regulation will overcome that basic expectation. This is also why this generation is getting de-banked.

The end result of this is that banks, being the slow, calculated, and risk-averse organisations they are, will likely allow disruptors the opportunity to come into the space between the bank and the consumer as a "friction-eliminator".

Utility and service are the new differentiators

As the four phases of disruption occur, the old differentiators of banks evaporate.

In the past, retail financial institutions held that **Product, Rate** and **Location/Network** were the mechanisms by which they competed. But in a transparent, open world where information flows freely—products are just a commodity. In a low-interest-rate environment, a 25-basis-point differential is hardly something to write home about. And if I never visit your branch except once or twice a year, it's hardly going to be the linchpin in my choosing your bank over a competitor.

It's far more likely that your mobile capability, your internet banking support, and the ease of use in onboarding and day-to-day problem resolution will drive my decision to commit to your bank. Ultimately, I'm not going to stay your customer in the hyperconnected age unless you provide me with great total-channel service.

Think of it this way. If you're dependent on me visiting a physical location to get a great customer experience or service from your brand, you're seriously disadvantaged against a brand that has contact with me 10 times a week through a digital channel. If you are relying on the branch to keep me happy, you've already lost the battle for the customer of today.

What all this is teaching customers is that they can have control, and they have choice. No longer will customers stay with a bank just because it is the first bank they ever took a deposit account with, or because it appears too hard to change. Those protections will no longer be afforded to a service organisation that doesn't *serve* its customers.

As I move my day-to-day relationship to a mobile wallet hinged to a bunch of value stores that give me the functionality of a basic bank account—but none of the KYC hassles—the banking sector loses a vital platform for relationship development. As a consumer I get all the utility of payments, and basic banking (cash withdrawal, online payment, bill payment, etc.) without the need for a specific banking relationship.

Why do I go to a bank ultimately? There are three core expectations—my money is safe, and I get access when/where I need it, and, as my financial behaviour becomes more sophisticated, the bank can facilitate my financial life through access to credit and advisory services.

I want to be in control, and when I need it, I expect rapid and seamless delivery. Don't ask me to fill out an application form with all the same details you've already asked from me four times in the past three years—I am not here to work for you, you are here to work for me. Don't ask me to wait, I am impatient. Don't dictate to me that I have to go to the branch to do this because I now know that is simply not necessary for a progressive financial services provider with the right systems in place. Understand me, so that you will know what I need before I do—you're the experts—you tell me. When you recommend a solution to me, don't treat me like a novice—be prepared for me to be well-informed and know more about the alternatives than your staff. Tell me why you are recommending this product, and how it fits my needs.

Deliver to my criteria. I'm the customer. It's my total ***experience*** that matters.

KEY LESSONS

Customer behaviour is rapidly changing due to two key factors, namely the psychology of self-actualisation, and technology innovation and adoption—otherwise known as diffusion.

Banks can either try to reinforce traditional mechanisms and behaviour, or they can anticipate changing behaviour and build accordingly.

The pace and rate of behavioural change is speeding up, not slowing down. Thus institutions get less time to react and anticipate the impact of such changes on their business. The longer institutions wait, the bigger the gap between customer expectations and service capability becomes.

There are four key phases to these behavioural changes and we are already at the third phase, and it is the game changer—the loss of physicality and the mobilisation of payments. The fourth phase, the unhinging of the basic bank account from the bank, will occur gradually over the next decade, and banking will never be the same again because banking will be everywhere, and anyone can provide the utility of a bank. The rise of the "de-banked" is evidence of the growing trend of consumers who value the utility of banking over banks themselves.

When the world's bank account is a mobile phone—who exactly is the bank?

Keywords: Countrywide, MyRate, Merrill Lynch, Charles Schwab, Lead Generation, Psychology, Customer Experience, Unbanked, Underbanked

Endnotes

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2 The ROI of Great Customer Experience

As we've already identified, we're seeing a sea-change shift in banking behaviour. Behaviour that will flip on its head, change typical interactions and channel preferences of the day-to-day bank relationship. Behaviour that will render irrelevant many of the processes, constructs, business rules, metrics and systems of the current retail bank. Behaviour that will redefine what it means to be a bank and to provide banking services. Big statements? Yes, but simply consider behaviour around day-to-day banking experiences.

By 2016, the average retail banking customer in the developed world will interact with a bank as follows[1]:

Retail Banking Channel Interactions 2016 Est

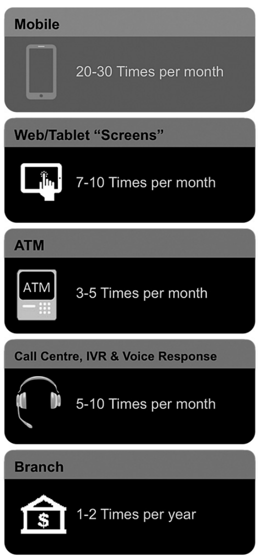

Figure 2.1: Customer experience is primarily a digital endeavour from this point forward

This means your customer experience—the way your brand interacts with your customers—is primarily defined not by an investment in people, but by an investment in technology.

It is conceivable that as a customer I could interact with you 500 times a year via mobile, web, tablet and ATM, and that I could actually speak to someone from your bank fewer than five times in an entire year. The average retail banking customer will visit your branch maybe twice a year, or, as an outlier, perhaps three to four times a year.

Back in the 1970s, as the customer, I had just one channel to interact with—the branch. Even when I called the bank, I called my branch manager. Then along came the call centre and ATM machines in the 80s and early 90s. Banks tacked on call centres to enable me to talk to someone, and answer simple questions. The ATM allowed me to get cash without a teller. Then in the late 90s the Internet arrived and changed things radically—I could do much of what banks did in-branch, online. The only things that perhaps prevented more widespread use of the Internet were system limitations, process and compliance rules, not necessarily adoption.

Throughout all of this, banks have maintained that the branch is central to banking, but in the face of the above projected mix of interactions in the next few years, that position not only isn't logical, it is a recipe for economic disaster. In fact, it doesn't make sense at all. There can be no metrics or data that can possibly substantiate a branch-led view for retail banking in light of such radically different day-to-day banking behaviour.

If as a bank you are hoping that one or two visits to your branch network are enough to hinge the entire customer experience, loyalty and relationship on… you're absolutely screwed.

Firstly, if I'm your competitor and I've got a superior messaging strategy via digital channels, you can't even come close to competing with me on a relationship basis with your face-to-face channels. You might argue that those two visits are critical, that the face-to-face visit could very well be the foundation of the relationship the customer has with the bank. That sounds a lot like justifying the existence of the branch network instead of trying to build a great overall customer experience. If you were totally customer focused, then you simply wouldn't care which channel the customer chooses, you'd make sure it was the best experience every time, regardless. So how do you measure, and thus improve, a total customer experience for the brand, across a channel mix that is largely digital?

In the past, when banks measured customer satisfaction, they'd do so by taking a customer survey in the branch. Later banks started *mystery shopping* the competition to see if their competitors' sales processes were superior to their own within the branch. Later, customer surveys were added via the call centre or snail mail to try to get more of a feel for the brand's performance. Then management tied in KPIs[2] to the customer survey—hoping for minor gains in the metrics of customer satisfaction.

Over the last few years, the industry has responded to this pressure by taking another look at channels and the way performance is measured—are customers waiting too long to have their calls answered? Would IVR systems lower the load for high-frequency enquiries? Are ATMs located in the right places? Will customers find them? Who is using the Internet, and what do they want to do online with the bank? Do you need to provide product applications online? Do you need apps?

Can retail banks integrate the banking experience better into customers' daily lives, for example by allowing them to sign up for car financing at the dealer, rather than having to come into a branch and insisting they treat it as a separate transaction? Could mini-branches or sales offices be positioned at locations and open at times more appropriate for different customer groups? Some of this analysis was cost-driven; other initiatives were marketing-driven. These piecemeal changes have only served to create some isolated improvements in the overall customer experience. Let's examine why.

Firstly, the **channels are still in silos** that discourage sharing of customer learning and, as a result, some of the most remarkable service opportunities go missing. Secondly, the **organisation structure and traditional business models frustrate change**. The most significant problem, however, is that all these changes are happening in isolation of the customer in most cases. **Customers are rarely involved** in the proposed solutions put forward internally within the institution. Let's discuss these three areas.

Channel silos

Customers don't use channels or products in isolation of one another. Every day customers will interact with financial institutions in various ways. They might wire money to a third party, visit an ATM to withdraw cash, go online to check if their salary has been deposited, pay a utility bill, use their credit card to purchase some goods from a retailer, fill out a personal loan application online, ring up the call centre to see what their credit card balance is, or report a lost card. If they are sophisticated customers or clients, they may also trade some stocks, transfer some cash from their Euro forex account to their US dollar account, put a lump sum in a mutual fund, or sign up for a home insurance policy online.

In the early days of the Internet and call centre, it was not uncommon to find that the call centre and internet banking were 24 hours behind the in-bank systems because the "batch" processes that updated the alternate channel databases/logs ran overnight. Thus, if I made a transaction via an ATM or through the branch, it wouldn't show on my online statement or could not be verified via the call centre until the next morning.

Today, my internet banking account view can show me that my available credit card balance is US$10,000, but because of transactions that don't yet appear on my statement, my actual available balance could be $250. When I try to get a bank to explain this discrepancy, they'll try to argue that those other charges are "pending" processing by the merchant or card issuer. For me as the customer, the problem is that I can't use more than $250 before my card acts as if it is maxed out.

The technical challenges to creating an integrated channel infrastructure from a transactional perspective are largely due to the fact that new channels have been added onto mainframe legacy systems that were simply not designed to work in real time, across a distributed architecture.

The more significant problem is that the owners of these disparate channels rarely, if ever, talk to one another. In fact, in most instances, the different channel owners view the others as competitors for budget dollars, customer mindshare and share-of-wallet. This spills over to product teams, where teams regularly compete against one another for customer attention.

There are rarely metrics or incentives that encourage silo owners to promote their internal competition, or to serve the customer ahead of revenue.

To illustrate the silo problem, I'd like to share an experience I had as a customer of a retail bank in Hong Kong a few years ago. At the time I held a Gold Visa credit card, but had recently been sent an invitation to upgrade to its Platinum Visa credit card product, along with a "pre-approved" application form. I was happy with this and was ready to sign up, but hadn't had the time to fax off the application form (why couldn't I do this online, I thought?).

About 10 days later I was in a retail shop purchasing a Persian rug for our apartment, and I got a call from the bank. They were querying the purchase, the equivalent of about US$5000, because it was an unusual one-off purchase for me to make. I confirmed the purchase over the phone, the transaction was authorised, and I was then told by the CSR[3] that the reason they were calling was that some Gold Visa cards had recently been compromised. They then suggested that just to be safe, they could reissue me with a new Gold Visa credit card to ensure I was properly protected. I could pick it up from my branch in two to three days' time.

I agreed to their suggestion and thought it was proactively a positive move, but I asked them to reissue me with a Platinum Visa card instead as the bank had sent me the pre-approval offer just a few days earlier. There was silence at the end of the line, followed by the CSR telling me, "I'm very sorry sir, the Platinum Visa Credit Card department is a separate profit centre within the bank—we are not related." I suggested that maybe the CSR could call the Platinum department and explain the situation and ask them to issue the card, and I would fax the application form to them as soon as I returned to the office. The answer was, "I'm sorry, sir. I wouldn't even know who to call. I don't even know if they are in our building…"

From a customer experience point of view, this was a total, unmitigated disaster. As a customer if I wanted a solution to this problem, my *only* choice at this point was to do all the work resolving it myself. I would have to ring the Platinum credit card department and explain the issue, fax through the form and wait for the new card to be delivered. In the meantime I would have to cancel the Gold card myself, and work out how to transfer the balance from the Gold card to the Platinum card. This would probably mean at least one but probably a couple of trips to the branch. Why?

The problem with this structure is that the primary measure for these business units or profit centres remains the acquisition of new customers and the retention of existing customers. The Gold Card team would actually be penalised on a performance measurement basis by recommending I take the new Platinum card. There was no incentive to transfer me over to the new product because their numbers would take a hit. It was in their interest only to do everything possible to retain my account within their product silo, regardless of whether this was best for me or not. The business rewards such profit centres for isolating customers, and categorises activities that holistically provide a better all-round service as inefficient, or worse, irrelevant.

The same thing happens frequently with customer channels. Although those teams mostly do not actively set out to isolate customers, they end up ignoring the rest of channel activity as irrelevant to their part of the world. Call centre teams don't talk to Internet teams, branch teams don't talk to call centre teams. IT, PR and marketing teams frequently battle it out for control of the web channel. Email marketing and push-mobile services are handled on an ad hoc basis, resulting in no one taking control of messages that ultimately reach the customer. Legal and compliance teams frequently hinder channel teams from simplifying application processes through new channels because of a conventional view of the world. It's a mess.

If the institution were to step back from the day-to-day operations and actually look at how a customer interacts with them, they'd realise that from a product, process and channel perspective, the customer is totally agnostic. They just want to get their banking task done…

Customers choose the right channel at the right time for them, depending on a number of factors, such as time constraints, availability, complexity and the availability of a "deal".

What customers *don't* do is think, "I think I'd like to go to the branch today to process that travel insurance application…" They think, "Hey, I forgot to renew my travel insurance and I'm travelling on Friday. Where am

I going to get this done before I have to travel?" If they are comfortable with the web, they might log on right there and then and apply. Alternatively, they might ring the call centre and see if they can sign up over the phone. Or they might call their travel agent or visit their airline's website and see if the airline/hotel package they have has some travel insurance deal linked to it. In the world of banking as a utility, however, they'll have the option to bundle travel insurance with their trip they purchase, or they'll receive a geolocation- and time-sensitive notification via their phone as they walk into the airport ready to depart on their trip.

So why aren't institutions taking a customer behavioural approach to this instead of building silos in isolation? The main issue is an organisational structure that is still built on the concept of branch-based transactional banking at the core, rather than a multichannel or a customer-led approach.

HOT TIP: Guaranteed to reduce your call centre and IVR load by at least 15 per cent this year…for the average bank more than US$1m in savings…

Channel silos cost banks money because they duplicate functionality and services around customer interactions. If you were a customer and you needed an answer from your bank, how likely would you be seeking assistance today? Most customers will fire up their browser on their office or home computer, go to the bank's website, and try to find the correct phone number to answer their query. If you're a bank, here are a few tips to reduce costs and improve customer satisfaction, based on better understanding customer behaviour.

- Don't discourage customers from calling you. You might think by hiding phone numbers on your website you save costs by reducing call centre load. Research shows, however, that if you can direct customers to the correct call centre number quickly, you reduce traffic and costs—rather than leave customers to experiment by calling many different numbers.

- On every product or transaction page on your website, list the specific call centre number for that type of product/service. This can direct customers to an Interactive Voice Response menu specifically designed for that query, which will reduce call centre load and ensure CSR (customer service representatives) are appropriately equipped to answer specific questions.
- Even better, put a Skype calling button on the website where they can contact someone from the bank as they have a question, rather than waiting for them to find the correct number and call you separately. UBank™ in Australia used this methodology with great success.
- Customers are already coming to your website to find the solution, so why not put a list of the most frequent call types, issues or questions in the same area of the site where customers look up the telephone number? Even better, why not put the same list on the homepage!
- Compile this list of these "top" service enquiries by checking call centre data for the most frequent call types over the last six months. By simply putting the answers of these frequent issues on the site, you can reduce call centre traffic by 10–20 per cent.
- Keep in mind you would actually have to provide a solution on the site, and not just some FAQs. There may have to be some process intelligence. But get this right and those customers *already* going to your website to solve this problem will not ring your call centre. Thus, immediate load reduction…
- Remind customers when they withdraw cash from an ATM that their credit card payment is due.
- Ask customers if they'd like their account balance sent by SMS to their mobile phone. By SMS-ing customers their account balance, you reduce transaction load on the ATM network for customers who withdraw cash and then recheck their account balance. With 20 per cent of call centre enquiries typically related to account balance, imagine what reduction in call centre load would be possible with SMS and mobile apps providing the balance.

Banks should not so much be looking for channel migration opportunities as simply looking at which types of transactions work best on which channel, given a set of circumstances customers might find themselves in. Doing this in an integrated fashion so the customer gets an overall view of the institution is far more important than just blasting individual offers down a new pipeline because the technology allows you to do so.

While revenues, application numbers and transaction activity help compare performance year-on-year and against competitors on a balance sheet basis, aggressive, non-traditional competitors are entering the financial services arena without these preconceived notions. As early as 1994, Bill Gates made the statement that "Banking is necessary, but banks are not."

"Banking is necessary, but banks are not." *Bill Gates, Microsoft chairman, 1994*

Institutions will need to adapt and change and find new ways of working, or give up market share. Yes, many of the traditional "functions" of the bank are now being handled by intermediaries, specialist providers and non-bank institutions. Within the Bank 3.0 paradigm, this disruption to the traditional model of banking is only set to accelerate.

Organisation structure

By examining the behaviour of customers, the glaring realisation is that institutions are essentially assuming that customers only ever use one channel at a time to interact with them. Hence, it is not unusual to find a web team that believes that it can take 30–40 per cent of branch traffic and service it online. Likewise it is not unusual to hear proponents of branch banking telling you "the branch is back" and that the winning strategy is to be investing in more real estate and variations of the branch to retain customers. It's also not unusual for customers to receive dozens of direct mail offers, email marketing offers or SMS promotions from different "revenue centres" within the bank, independent of one another.

Today, 95 per cent of daily transactions are done electronically[4] and, in most cases, most of the transaction volume comes through direct channels, namely the ATM, call centre, mobile and the Internet. By February 2007, HSBC in Hong Kong had reported in the *South China Morning Post*[5] that 90 per cent of its daily transactions were through the phone, the Internet or ATM, leaving the rest to branch. RaboBank, FirstDirect, INGDirect, UBank and others have been able to operate successfully without any reliance on branch structures. This is not a criticism of branches, because I believe that branches will remain an essential part of the future of banking. However, look at the organisation structure of most banks today and you'll see a complete and total lack of understanding of customer behaviour inherent within the organisation chart. It's really quite appalling that the organisation structure of most banks has not caught up with this reality of consumer behaviour.

When we examine the organisation structure of most retail banks, the Head of Branch Network is second only to the Head of Retail and, in many cases, is a direct report to the CEO. In contrast, the manager responsible for the Internet often sits under the IT or marketing department, three or four levels below the organisational equivalent of the branch business unit head. So let's get this straight. Ninety per cent of the transactions go through channels that are managed by managers who have only a modicum

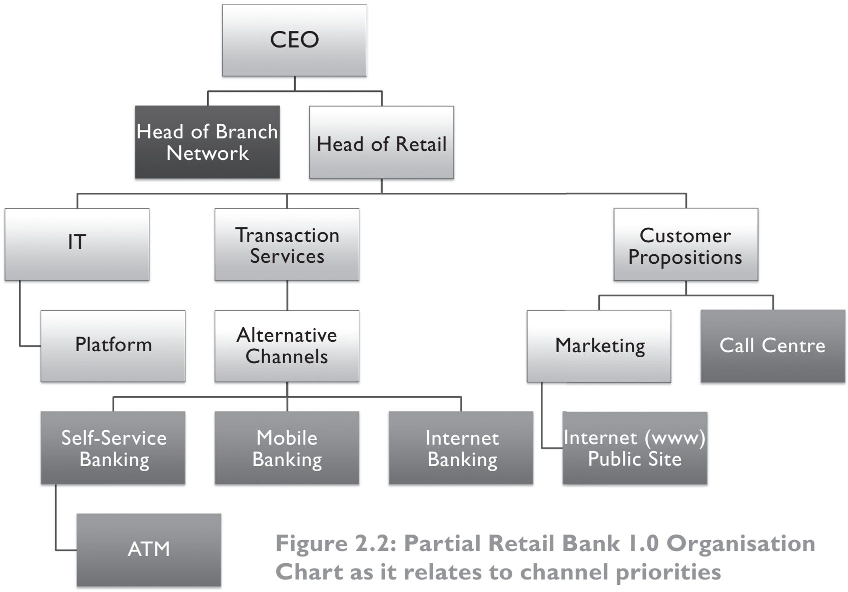

Figure 2.2: Partial Retail Bank 1.0 Organisation Chart as it relates to channel priorities

of influence within the organisation structure, while the head of branches has the ear of the CEO yet looks after just 5–10 per cent of the daily transaction traffic within the bank.

That doesn't even start to address the fact that mobile will be your number one day-to-day banking channel in just four years and you probably don't even have a separate Head of Mobile function, or the fact that 50 per cent of your customers are on Facebook and Twitter and you still don't have a Head of Social Media. That shows organisational priorities that don't relate to consumer behaviour.

"Ah, but the branch generates all the revenue…" we've heard it argued. This is a really good justification for keeping traditional structures in place. Well let us examine if that is really the case.

Let us take credit card acquisitions as an example. How do you market credit cards? Currently you might use direct mail, newspaper advertisements, web and possibly promotional marketing offering a "free gift" if clients sign up for a new Visa card or MasterCard. Customers are then faced with probably two or three choices on how to apply. The first option is that they can phone the call centre, but the call centre refers them to the branch because they need to present proof of income and proof of identity to an officer of the bank. The same might be the case for the Internet, where the application form can be filled online, but you then call them and ask them to come into the branch to complete the application.

Who gets to record the revenue for the credit card application? Not the call centre, or the internet channel, but the physical branch that executes the final signature on the application form and the Know-Your-Customer compliance check on the proof of income. Yet the branch actually has had practically zero involvement in the sale and is simply just a "step" in a required adherence to an outmoded compliance process. So does the branch actually generate the revenue, or does it merely handle the accounting?

The attitude of many retail banking senior executives seems to be that the branch is a serious banking channel, whereas the remainder of "alternative" channels are just that—alternatives to the "real thing". The problem is that customers simply don't think like this.

If as a bank you separate digital channels from other distribution channels today by calling them "alternative channels" or e-channels, then you don't understand that these are your primary channels today, and you are already out of touch with your customer base. Your organisation doesn't match the behaviour of your customers.

Customers simply don't assign a higher value or priority to the branch; they just see it as one of the many channels they can choose to effect their need for banking. In fact, many customers these days choose specifically not to go to the branch because they don't want to stand in line, or they find it troublesome to get to the branch at times when they are open. Admittedly the branch is a premium service channel, but it is not the *only* channel. In addition, how do I measure premium service? If you built internet and mobile channels really well, customers may even pay for the use of those channels in return for the time and service benefits. Why the growing gap in understanding?

Widespread dissatisfaction signals the need for change

One of the key problems that obfuscate the ability of the organisation to serve customers is the increasing adoption of bank policy in the name of risk mitigation or reduction. No greater an opportunity has there been to see this conflict of organisation and purposes than during the recent global financial crisis.

Bailout funds were an issue hotly contested and argued in the US, UK, EU, Australia and elsewhere as very expensive mechanisms for preventing a 1929-type global depression. There were consistently two arguments given for injecting capital into the ailing banking system. The first was that the asset-backed securities underlying the subprime bubble had become "toxic" and only by purchasing these toxic assets could the market come to terms with the ongoing factoring in of these assets. The second was that the crisis had created a liquidity and capital adequacy crisis for banks and that they could only free up funds for the general public if their liquidity was improved.

The first goal may have been accomplished although the long tail may yet still appear. The second goal was a failure with respect to customer expectations, however.

While banks achieved a welcome top-up that reduced their cash-flow problems, internal risk strategy dictated that in an economy in trouble, all but the very best customers represented too great a credit risk to chance lending them money. So banks started to freeze loan books, aggressively pursue those accounts that were having problems meeting their repayment schedules, and basically stopped all lending to those that needed it—small businesses and individuals. Small business activity and retail consumption are two critical levers in kick-starting an economy after a recession, thus bank policy on credit adversely affected the recovery cycle. In the meantime, as regulators got tougher on banks and investment firms, institutions sought to maximise fee and margin on lending products out of fear that regulation would restrict future options in this regard.

There was another significant factor here, though. In taking government money, many banks suddenly found themselves, within the space of a few months, cashed up. As they weren't lending to customers, what could they do with all this money? They invested it, of course. Based on the Warren Buffet school of successful investing, we all know that *reversion to the mean* was guaranteed to restore value to the markets once economic figures started to turn around, if only back to the historical averages. Most consumers weren't that confident—but the bankers know a good trading bet when they see one.

Margin-trading off government bailout funds, basically free money, created some healthy returns in the space of just six to nine months. So instead of using bailout cash to bolster lending to those that most needed it, banks used the funds to generate profit for the bank. Now, if this resulted in more dividends for shareholders and the relaxation of some of the bank policies on lending for consumers, then it would be a fair result. But instead bankers decided that as they had all done so well in investing this cash, that they deserved a hefty bonus for their hard work.

Customers understandably have not been impressed by such a brutal, net-margin-led approach to policy and bank strategy. Customers rightly expect the bank to act as a service organisation and to look at even more opportunities to provide support for customers during a period of economic instability. The customer response to the industry approach was overwhelming.

Since 2008 it is estimated that blogs extolling the negatives of banking have increased by more than 400 per cent. A specific campaign in the US, first covered by *Huffington Post* and then supported by major networks such as ABC, encouraged consumers to move their money out of big banks and into credit unions.[6] Customers angered by opportunistic credit card rate hikes and overdraft fees flocked to YouTube to tell others of their treatment. Obama, Cameron, Sarkozy, and other leaders criticised the "fat cat" bankers and their bonus schemes, even slapping heavy tax penalties on future windfall gains.

Things haven't subsided for distraught bankers more recently. In 2011, Kristen Christian, an art gallery owner in Los Angeles, California, said she was dissatisfied with Bank of America's "ridiculous fees and poor customer service" and created an event on Facebook called "Bank Transfer Day",[7] inviting her friends to close their accounts at big, for-profit banks and move their money to credit unions and local community banks by 5 November 2011.

BofA became the poster child for "ignorant and arrogant bankers" when they tried, unsuccessfully, to levy a new $5 account fee to reduce the impact of the so-called Durbin Amendment.[8] Between 29 September, when BofA introduced their new fee, and 5 November (Bank Transfer Day), the Credit Union National Association reported $4.5 billion in new

Figure 2.3: The poster for Bank Transfer Day on 5 November 2011
(Credit: BankTransferDay.org)

deposits[9] and 440,000–650,000 new customers—a 50 per cent increase in new accounts.

Customers are seeking alternatives to big banking because they believe that banks have lost touch with reality and don't care about their customers anymore … and they'd mostly be right. EPS (earnings per share) and margin have long become the drivers for large, listed financial institutions.

Avoiding risk and making profit for shareholders dominate the thinking of the modern commercial bank today. What has been lost is the balance between this and servicing customers. This imbalance has been institutionalised as banks make excuses for why things don't work the way they should for customers.

Banks argue that processes are the way they are to protect the institution (and customers) from risk—when often the processes are just bad, unwieldy and massively out of date.

Banks cut back on new innovative areas or substantially underinvest in technology such as mobile or social media, but maintain horrendously expensive branches that customers hardly ever visit anymore. Then certain bankers argue vehemently that branches need to survive. All the while customers are flocking to mobile and tablet computing faster than ever before.

So how do banks respond generally? We hear the industry say that social media, mobile and the Internet are not secure and this is the reason for using caution when introducing these new technologies. Meanwhile banks are still sending customers statements and credit cards in the mail—a channel that is so easily corrupted and so insecure that it is laughable.

The problem isn't the global financial crisis, Durbin-response fees, or even bank bonuses. The problem is there is simply too much momentum or inertia in the current system of banking and, as such, the gap between customers and how they behave, and how the institution behaves, has become almost insurmountable.

If retail banks want to stay in the game, they need to start behaving fundamentally differently—starting with re-engineering the customer experience and putting a new management layer in place that embraces continual change.

The Branch versus Online versus Mobile debate

Staggeringly, recent research released by Google shows that when it comes to financial products, up to 88 per cent of customers today in developed economies start their journeys online.[10] For deposits and credit cards, 78 per cent of time spent researching options overall is done in the digital space for an average of 3 hours and 20 minutes (that's up from 58 per cent in 2008). For mortgages and home loans, 62 per cent of their overall research is done online for a period upwards of 11 hours and 25 minutes before a product is settled on. Some 77 per cent of those surveyed said that they didn't know about the product they finally chose prior to starting the task.

This data shows a significant shift in behaviour when it comes to the selection process. Traditional marketing theory suggests that brand marketing and campaign marketing are strong influencers of behaviour when customers are selecting products, but this most recent data flies in the face of accepted theory. Fifty-one per cent of customers had a preferred brand when they started, but of those who used search to attack the task, 58 per cent *did not* search for their preferred brand! Of those who started with a preferred brand, 31 per cent ended up selecting a different brand.

> "Customers will consider an average of 4.5 banks, but will only shortlist 3.4 products for more detailed evaluation. 31 per cent of customers with a preferred brand ended up selecting a product from a different bank online…"
>
> —Karen Grinter, principal client advisor with Global Reviews (November 2010), Google Think:Banking sponsored research

So what about the role of the branch, call centre, and other channels in the actual application process? Sixty-eight per cent of those surveyed *prefer to apply online*, compared with just 29 per cent who prefer the branch experience. However, 89 per cent of the people said they are open to applying online in the future if banks and FIs get their approval processes up to scratch. That's pretty much everyone. So if that's the case, why don't more people apply online for financial products, and why isn't there an absolute abundance of evidence to show the ROI of online onboarding and fulfilment?

Research consistently shows that poor usability is the primary reason customers abandon a website, leave, and then pick a competitor's brand or product online. The same Google study previously referenced shows that the highest percentage of customers who stay with online throughout are in the $100k+ p.a income bracket. In fact, the study indicated that for 82 per cent of High Income customers, *total research* is done online today and 74 per cent of these indicate they would *prefer* to apply online for products such as deposit accounts and credit cards.

I've worked extensively with many major brands, and there are almost no global brands in the banking arena that have a dedicated usability or customer experience team designing these critical interactions and online processes to streamline or improve customer acquisition. Of the big four banks in the US today (BofA, Citi, Chase, Wells), the only banks that have put any work into the homepage experience recently are Citi and BofA. The homepage is a hotly contested property in most banks today, with every product team in the retail bank (and in some cases the whole bank) competing to get their hyperlink, product promotion, or anything else on the homepage. This is entirely counterproductive as it clutters the homepage and results in the risk of high bounce rates (we'll talk more about this in later chapters).

When we type in "Savings Account" or "Checking Account" into Google, we do get some optimised product selection experiences, but SEO (Search Engine Optimisation[11]) is still a challenge for many of these brands. Given the critical nature of online in brand selection, one would think that there would be millions of dollars a year spent on optimising the customer journey, but in most cases there have only been incremental improvements over the last five to six years. Overall, the utilisation of the web channel in retail financial services is appalling. Starbucks, Apple, PayPal, Amazon and others are two to three generations ahead of most retail banks in their level of competency online.

In 2012, there are massive changes in store on the margin and engagement front. In the US alone, it is estimated that there will be a $25-billion shortfall in fee income stemming from new regulations,[12] and a $50-billion margin shortfall as flat rates persist.[13] Meanwhile banks have not been able to right-size their operations as consumer behaviour has shifted. As customers rapidly move online, how do banks lower operation costs in branches that are suffering from dwindling support while maintaining the service commitments they've made in the past?

In today's retail financial services environment, branches, in-branch staff and agents are not the ones selling the product. The brand is. Retail financial service brands today are a collection of experiences, increasingly defined by multichannel interactions and customer discussions and debates in the social media space. If processes are biased towards the acquisition of customers or sales of products in-branch or face-to-face, then it would be very easy to argue that a contemporary retail financial institution has no idea how the customer of today engages a brand.

So how well do institutions know the flavour and depth of multichannel interactions with their brand? Generally, in my experience, most don't have a clear understanding of the mix of interactions because each channel is measured in isolation. There is no understanding that channels are related to one another because the organisation structure reinforces a one-channel-at-a-time approach to strategy.

Most banks could say which products they've sold through their branch(es) this month, and they probably track which products they sell directly online (if they have that functionality), via the phone, etc., for revenue purposes. However, if I asked the average retail banker to tell me which are the best products to sell through their internet channel, what would the technical basis of that answer be? If I were a banker looking at how to generate new revenues through my IVR or ATM channels, how would I figure out the right sales pitch and implementation? If I were trying to understand at what point a mortgage customer switches from researching a product online to ringing a call centre or visiting a branch, most banks would not even be in a position to tell me that the customer had first looked at their website, which actually led to the sale. This is the really critical stuff—the why and how of consumer behaviour.

There are two critical questions here that we will delve into in much greater detail later. The first question is, if the institution puts a product on a specific channel, will the customer engage them on that channel for that product? The second is, what is the best method to implement the solution so you get maximum take-up or utilisation? To be very specific, I'm not talking about origination, segmentation or marketing mix here. I'm talking about which product or service works on which channel, how simple it is to access for a customer, and how you measure that.

Although long-held traditions are slowly changing, bankers tend to consider the branch as the premier day-to-day banking channel, the Internet as a transactional channel with incremental revenue opportunities, the mobile as a smaller version of the web with respect to transactions, the ATM and contact centres as cost centres with limited cross-sell revenue capability. But that doesn't match how customers engage or how they use these channels.

Most developed markets research shows that customers consider the web their primary day-to-day banking channel, the mobile a rapidly emerging support channel, and the ATM where they get cash—these are daily occurrences, the staple of the banking experience. The call centre is what they call when they've got a problem, or when they can't find what they need online. The branch is where they go when they can't do their banking through the other channels due to process or bank policy, when they need a particularly sticky problem resolved, or when they need advice—and these instances are likely to occur fewer than three or four times a year.

If retail bankers viewed the world the same way as their customers, what sort of channel prioritisation would there be today? Take major brands in the space such as BofA or HSBC, each of which spends north of $1 billion on their branch networks and approximately $50 million on web and mobile banking annually. Ironically at the time of press HSBC still doesn't have a mobile app for most of its customers. In the worst case, the split of this spend should look more like $250m on web and $500m on branch today, even considering the relative cost performance of the channels. Let's not even start talking about social media. Today's spend just doesn't make sense given behavioural economics.

Go back and look at your retail channel budget today and figure out how to put at least 30 per cent of your total channel budget into the mobile, tablet, and web. Then you might just be getting closer to an organisation chart and budget mix that is closer to what your bank needs to support customers in the near future.

Which product works best on which channel?

Let us begin by making certain assumptions that relate to the complexity of the product. Obviously the more complex a product, the more handholding the customer might need to engage in that product. By law in some jurisdictions, certain investment products, for example, require a customer to be advised on the risk involved in that type of investment product. In other instances, a customer may have a plethora of choices and simply not know the right product for his particular circumstances, say, in the case of life insurance. A mortgage product is generally considered a pretty complex product (although increasingly commoditised), so it is a reasonable assumption that at some point before a customer receives approval, he's going to have to talk to a member of the mortgage product team to decide on the right option(s).

An April 2011 report by EFMA and McKinsey & Company[14] bears out this relationship between complex products and the need for advice through face-to-face channels. The report, based only on the European retail banking sector, included 3000 end-consumers, an online survey, and 150 banks. It clearly shows that for less complex products, the shift to so-called "direct" or "remote" channels occurs considerably faster.

The report identifies a number of key shifts in behaviour. Data from 2010 showed a growing percentage of consumers who stay away from the branch entirely. In 2010, 50 per cent of the Netherlands' population had not visited a branch, and in France, Germany, Italy, and the UK, those figures were upward of 20 per cent. Predictably, younger consumers (aged 20–35) were earlier adopters in the multichannel cycle than their older counterparts. When it came to product purchasing, however, there was a clear expectation that "direct channels" (Internet/ATM/Mobile) would become increasingly critical for engagement and sales.

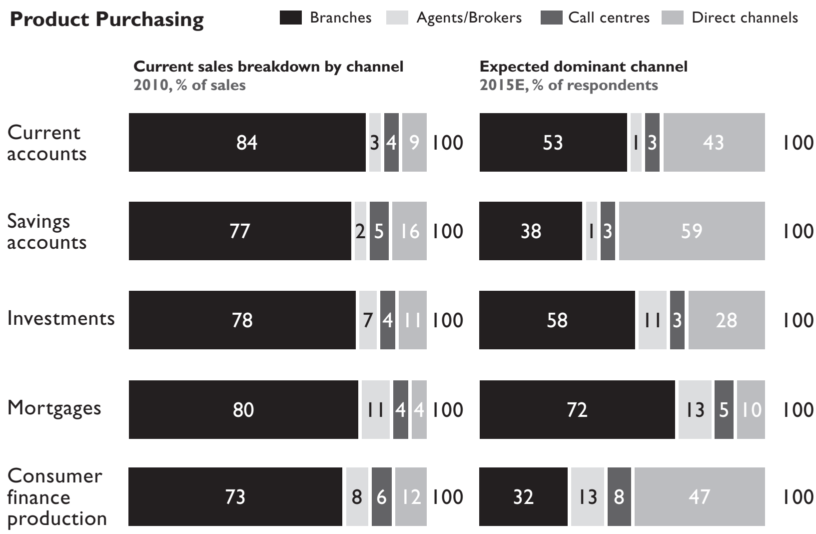

Figure 2.4: Product purchasing by channels, 2010 vs 2015E
(Source: EFMA online survey across 150+ European banks)

So investment products, life insurance and mortgages all require a face-to-face interaction right? Well, it's not as straightforward as that.

The above research almost completely contradicts Google's earlier findings. In fact, there's almost no correlation with real consumer behaviour in terms of research that leads to a product purchase. How can Google claim that 88 per cent of Internet users start their journey looking for a mortgage online, while EFMA/McKinsey say 80 per cent of consumers apply for a mortgage through a branch?

The problem is twofold. Firstly, banks don't measure the entire journey or engagement of the customer from interest and research through to selection and final application/purchase. It's simply no longer a single-point-of-contact world when it comes to sales today—it's a journey, a collection of experiences and interactions that leads to a sale, or hopefully to a relationship. Secondly, even when a product is sold online, revenue is often allocated to the "home" branch of the customer so that it skews internal metrics, and management doesn't even get an accurate picture by reviewing revenue. Thirdly, for a new customer, KYC and compliance rules in the EU still dictate that the safest option for the bank from a risk perspective is to deal with the customer face-to-face to ensure they can confirm his identity, etc. So, even if I want to apply online, I can't if I'm a new customer and the bank determines that I need to be seen face-to-face to confirm I am a real person, with a real identity. So I'm forced into the branch, and this becomes a "false positive" for branch acquisition.

Thus, I submit to you that the EFMA/McKinsey study is significantly flawed. It doesn't represent actual consumer behaviour, but represents more of a collection of metrics and compliance processes. It is based on one piece of data—where did the final step in the compliance process take place? It doesn't measure the journey.

Google's study is more representative of behaviour because it is measured in real time, as people search and engage when they need a financial product. The concept that a customer would choose the branch over the Internet doesn't really work in the case of a mortgage because the fact that the customer has applied for a mortgage in a branch has almost nothing to do with the selection process he used earlier online before walking into that branch. The key problem is this:

We need to measure accurately the total journey or engagement of the customer end to end, not just the last step in the journey.

As a customer I may very well use the Internet to research my investment options, so before I go to the advisor in the branch, or he comes to see me at my office, I may very well have decided the asset classes I want to invest in, the investment horizon, the level of risk I am prepared to take. I may have gone online and used a risk profile questionnaire to see what level of risk I will tolerate. I may have used websites or magazines on investments to look at whether it is the right time to invest in my local property market, or in blue-chip banking stocks. I may be part of an investment club online; I may even have my own online brokerage account separate from my retail bank. So while I may engage with an advisor in the final stage to execute a transaction, I may have already made the all of the critical decisions long before my meeting with the human advisor.

So while you can assume that for many customers, the *execution* of a complex product might occur through a human interaction, you cannot assume that this is the sum total of contact the customer will have regarding that product.

You have to understand which channels are used by which customers at what time, and at which stage of the purchase cycle or decision they are at. You need to cater for all of these interactions simultaneously. The good news is that for simpler products it is somewhat more predictable. So which products work best through direct channels? The answer is… it depends on which market and demographic you are looking at.

Below are some good results from a collection of 2007–09 surveys on Internet usage, where customers were asked the likelihood of their purchasing or applying for the following products online in the future. The results below (aggregated from 45 countries globally) show only those products where 40 per cent or more of those surveyed indicated that they would be *likely* or *very likely* to use the online channel to purchase or apply for that product type in the future.

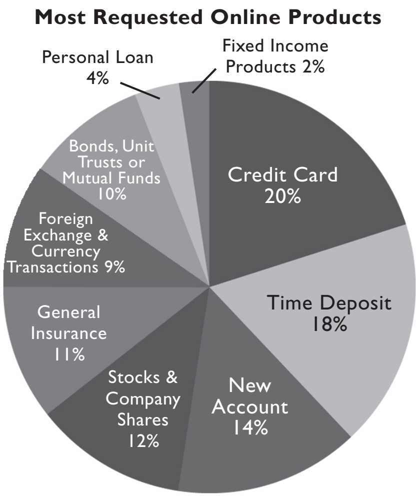

Figure 2.5: Preference for retail banking products online, by market[15]

We do see a pattern here. With the exclusion of the investment and trading products, all of the other products are pretty simple, namely credit cards, general insurance products, personal loans, time deposits or fixed income products, and opening a new bank account. These are also things you know work through the online channel.

Breaking bad inertia

I'll discuss this more in Chapter 11, on Engagement Banking. However, the key to understanding which channel is the right channel to push a product to a customer is understanding their behaviour around these products.

Every retail banking, investment or insurance product today fills a consumer need, based not on the product itself, but on the underlying utility of the product, i.e. what it is used for. As we discussed before, people don't buy a mortgage—they buy a home. They don't get a car loan or lease—they buy a car. They don't buy a credit card—they go shopping and want the ease of use at the POS. They don't invest in stocks or ETFs[16]—they look for interest from the money you're holding.

Financial services are all about the utility surrounding a customer's money, how that money helps him live his life. Think of retail financial services products as the financial glue that allows the consumer to live in a society where money, the flow of money and commerce are essential. Understand the context of the utility of the product, and the channel delivery options become clear.

When you get that clarity, the realisation is that increasingly we don't need a physical network or distribution point to maximise the utility and fulfilment of a product. That's the scary but very liberating truth.

The problem is that in the current environment there is massive inertia around "banking". Many banks today still insist on a physical signature card although regulators have generally not required that since 2001. Banks stipulate that the customer needs to bring in bank statements to qualify for a loan, even when he has an account with the same bank he is applying for a loan with. Even the language of bankers often needs its own dictionary—with terms such as draft (not a first edition of a document), telegraphic transfers (even though a telegraph is not involved), instructions (but not like an operating manual), annuity (what?), routing number, SWIFT code…

Breaking this inertia is just as critical as building great journeys or experiences for customers. This is where I'm going to challenge the legal and compliance professionals of the typical retail banking player today because to break the inertia, the internal processes or language today, you first need to get the change approved by the compliance or legal team.

I've often joked that compliance and legal departments in banks live in the Land of No. That is, the easiest and least risky thing to say when presented with a process or policy change is, "No, we can't do that." Why? Because the processes you've long established are proven mechanisms to mitigate risk in the engagement and onboarding of customers within the legal and regulatory framework you operate under as licensed or chartered financial institutions. Right?

Again, the waters are a little muddy here too.

Take for example the humble bank statement. About 15–20 per cent of customers in developed markets have already opted in for e-statements today, but that leaves 80 per cent of customers who still receive monthly statements in the mail from their bank[17]. I signed up early for e-statements hoping it would also reduce the amount of direct mail marketing I received from my bank, but I should have realised that this wouldn't stop them! So now 50 per cent of the mail I receive in my physical mail box is still from my bank, but it's useless direct mail that I never read.

Now imagine this scenario. Let's say we lived in a world where no one had ever sent paper bank statements and it was all done electronically (perhaps like our world 10 years in the future). Imagine a scenario where you go to the compliance department and present this as your brand new plan:

Banker: "So, we're going to print out all the transaction information on a stack of paper, and we're going to stick the customer's name and address at the top of this list of transactions, and then we're going to put the whole thing in an envelope and send it out to the customer. We think this will be great for customers to get all of their monthly activity on one document at a glance, a permanent record; *and* we'll be able to stuff the envelope with other offers and deals from the bank—marketing stuff to improve cross-sell and up-sell opportunities. The ROI on this promises to be very healthy!"

Compliance Officer: "So this is totally secure, right? The envelope you send is tamper proof, and the customer has to sign for it when they receive it? Like a registered mail or courier service?"

Banker: "Ah…no, not really. That would make it far too expensive. We're just sending it through the normal mail service, in a normal envelope—that's the cheapest distribution mechanism available. We want to do this as cheaply as possible, otherwise the numbers don't stack up."

Compliance Officer: "Well, putting aside that it would still be cheaper and far more secure to send this information electronically, who or how many people would have access to the envelope through this process?"

Banker: "Um, we don't really know, but it would probably be physically handled by a handful of people, maybe a dozen or so? We have our outsourced staff stuffing the envelopes, postal workers receiving and delivering the mail, and there are machines that do some of the sorting. Of course, there is the chance that on occasion the envelope might not get delivered to the correct address, but that's a very slim chance these days and we're sure that if someone received this in error they wouldn't actually open someone else's private mail from the bank."

Compliance Officer: "You're kidding, right? You want to take pieces of paper with almost all of the secure identity information we're fighting to protect daily from identity theft, you want to put it in a format that is totally unsecured, you will allow perhaps a dozen people to handle the document with no audit trail, and there's a risk that anyone in the chain could intercept that information either in transit or at the destination in the customer's mail box!? There's no way we're ever going to approve this! Why would you even think of bringing this to us?"

The problem with inertia around current processes is that you build up a false sense of security about these processes being somehow better for the bank, more secure, less risky, and less costly than something new. You even resist new technology plays over fears that this might compromise risk or security when, in fact, over time the existing processes have become more and more risky, more and more expensive, less secure and less customer-friendly. The value proposition a bank statement provided in the 1980s in replacing the passbook was clear. But today, it's an artefact that is costly, highly exposed, inflexible, and pretty much useless from a consumer perspective.

Given those facts, why don't banks start charging customers for receiving paper bank statements and give them the option of e-statements for free? That would make a lot more sense, wouldn't it?

The inertia in the system, however, would tell you that customers LIKE receiving paper statements in the mail, something tangible and real. But is that accurate?

Forrester Research reports from 2008[18] and similar research since show that the strong majority (at least 70 per cent) of consumers are willing to go paperless. The problem is that consumers are by and large lazy beasts, and if you require them to visit a branch and sign a piece of paper to move over to paperless, then they'll probably just let things lie. However, in just the same way (understanding consumer behaviour today), banks should realise that if they told customers that they were moving all online banking customers to e-statements on 1 January 2013 and, from that point on, if they still wanted a paper statement in the mail, they'd have to opt in and pay a monthly fee of $2.50—it's probable that most people would simply allow you to switch them over to e-statements automatically.

There's no other reasonable explanation for the lack of innovation around these sorts of processes other than simple inertia. Paper statements are costly, insecure, and inefficient at translating vital information about a customer's bank relationship. There's no regulatory requirement, cost or legal benefit in maintaining them. If you were designing a bank today from the ground up, you would never willingly design paper statements into the consumer mix. So why are they still around?

I've used paper statements to illustrate an existing case that doesn't make sense from a cost, compliance or security perspective, but there are likewise a gaggle of similar scenarios that are simply outdated—holdouts from an earlier generation of banking. Inertia that is currently in the system, but that will soon disappear, includes the paper application form and signature card, cheque books, bank statements as proof of income/spending, physical identity verification, ATM receipts, channel metrics (where they compete), etc.

And here are two more:

Account opening and administration

With average account acquisition costs being in the range of $250–350,[19] you would think that someone would have connected the dots between the need for a signature card (and related physical handling) at account opening, with the cost of acquisition. The easiest way to reduce acquisition costs is to get rid of the paper. Which brings us to annual costs for current/checking accounts too. With an average current/checking account costing around $350 a year, sending paper statements, printing cheque books that are never used, charging big fees for wire transfers so that you prop up your dying legacy cheque business, all smack of a business driven by inertia.

What's my account balance?

This is the number one requested piece of information from the bank today, and while you do provide internet banking access to this piece of information, the dominant method of a customer getting this is still through an ATM or through the call centre. A far simpler mechanism would be sending the account balance via a text message when a major transaction occurs, or at set intervals (say weekly), or as defined by the customer. The cost of sending a text of his balance to a customer 10 times a month is less than the cost to you of his one call to the call centre for the same information, and less than two of his ATM balance enquiries (based on current channel cost estimates). The deployment of mobile wallets will massively reduce these ongoing costs as well.

Why is inertia such a problem?

So here's the Achilles heel of banking today:

Inertia = Friction

This friction provides a reason for a seismic shift in core distribution and engagement. Risk modelling makes way for decision engines that are better handled as predictive or real-time rules than paper-based dependencies. Friction provides the impetus to replace old, worn-out processes with better engagement and experiences. Outdated paper requirements become a competitive weakness. The requirement for physical interaction dramatically limits scale. Start-ups that have no preconceived ideas or concerns over regulation push the limit without a care in the world…

As behaviour causes business models to morph, you'll also see massive shifts in organisational structure. The head of branch gets relegated to a line manager role for the channels team, on par with the head of internet, mobile and ATM banking, and contact centres. Customer engagement becomes a competency that transcends the typical push marketing capability, and advertising becomes a supporting tool in the engagement model.

To look at opportunities for removing the inertia and the friction in the customer experience, however, it takes redesigning customer interactions and experiences from the ground up, and it takes changing the way budgets are allocated.

When you give a manager a budget, she/he will do two things:

1. Attempt to prove that the return on that investment (budget) is really high, and
2. Attempt to ensure that next year's budget goes up (or at least not down).

These might not really be mutually exclusive points as #1 is used to accomplish #2. However any new channel in this mix suffers from having to steal budget away from existing channels—or, more accurately, from stealing budget away from the managers who run those existing channels within their domain. And that's a whole lot easier said than done.

The ability to rethink how customers will engage with your business in a channel-agnostic, real-time world takes a new skill set and new incentive programme. In the future, where differentiation is connecting to the utility of the bank and maximising service opportunities, you need to look to the science of interaction design. It's more than just user experience and

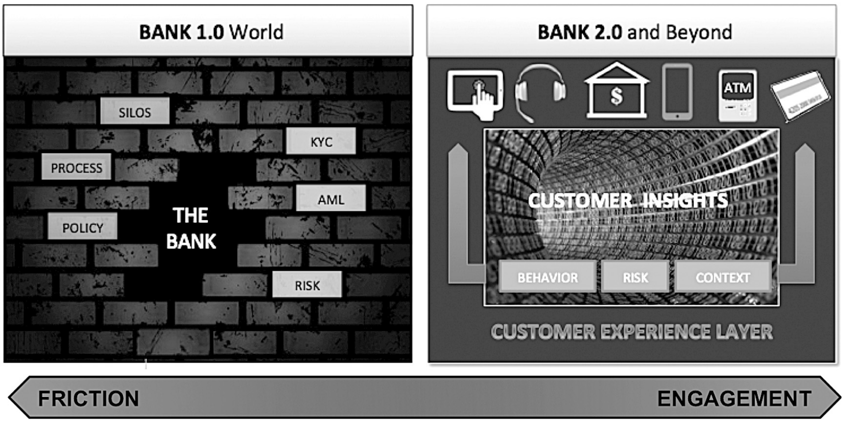

Figure 2.6: The new engagement layer attacks the friction in banking

interaction design, of course. It also requires seeding the design process with behavioural analytics, demographics, psychographics. It requires marketing and copywriting skills. It requires a messaging architecture. Most of all, however, it requires an intimate understanding of the behaviour of the customer.

The cost implications of not getting customers involved as early as possible in the design process are extremely negative, and while most institutions baulk at the upfront expenditure, the resultant losses due to poor design are much, much more expensive than getting it right in the first place.[20]

> "Since the Internet is very much a part of our lives today, consumers often conduct online research before making a purchase. Of the 500 adults surveyed in the UK, 88 per cent reported using the Internet for research while 94 per cent use it for shopping. This means that even for companies which aren't selling online, the web experience they offer visitors is key. Consumers visit a number of websites to find information and research a product or service before they make a purchase. This presents a golden opportunity for businesses to deliver a compelling and memorable interaction which will positively influence buying behaviour. By contrast, a negative online experience will elevate 'Web Stress' levels, causing customers to click away…"
>
> —CA Web Stress Index, 2009

> "The rule of thumb in many usability-aware organizations is that the cost-benefit ratio for usability is \$1:\$10–\$100. Once a system is in development, correcting a problem costs 10 times as much as fixing the same problem in design. If the system has been released, it costs 100 times as much relative to fixing in design."
>
> —Tom Gilb, "Usability is Good Business", 1988

So if you are a bank, how do you go about getting customers involved in the process? The initial involvement may be through focus groups or one-on-one interviews with key customers about what they need, but many banks are already doing this. The better approach would be to get them actually involved in the design process. Get them trying out early "lo-fi" prototypes of the interfaces and menu structures (IVR, Web, ATM) or get them to use the existing channels and observe them using those to evaluate the design problems before you embark on the redesign.

With usability tests and observational field studies, you can normally identify 80 per cent of the critical problems with just five customers involved in the testing process. That is hardly going to break the bank, as they say…

We'll talk about social media in Chapter 8 and the emergence of crowdsourcing and new approaches to brand engagement that play a critical role in financial services moving forward.

CONCLUSIONS AND KEY LESSONS

Customer experience is no longer the sole domain of the branch, it is the domain of the ***brand***. It exudes from everything you do, and customers are demanding a better experience, full stop. In fact, if I'm an average customer, I'm going to have access to your brand experience through an ATM, mobile phone or the Internet some 30–40 times more frequently than through a branch. If you're relying on the branch as the sole platform or measure for service excellence, you're totally screwed.

Inconsistencies in organisation structure and service levels between channels and silos frustrate customers who just want to deal in the most efficient way with the bank. As we will discuss in Part 3 of the book, the bank needs to do the following now to build customer experience:

- Appoint a customer champion to manage *all* channels
- Build analytics that identify failures in each channel or touch point
- Get customers involved in the design process, particularly with respect to the interface and language
- Create a team that trumps channel silos and managers when it comes to decisions around building better customer experiences
- Build a lab or crowdsourcing capability that engages the customer in an ongoing dialogue, and source ideas from this transparent platform
- Understand the total relationship the customer has with the bank across every channel

Customer experience is emerging as the new holy grail of retail financial services, but the key lessons are not so much about presence and service as they are about understanding the core needs of the customer.

To build an optimal customer experience, you must be able to measure how customer behaviour is adapting, and to measure the rate of innovation or value creation within the institution. This cannot be relegated to a channel-by-channel metric or approach. Channels and products don't compete for customer mindshare or share-of-wallet—they are now part of a complementary ecosystem, and in many cases, symbiotic.

While many institutions have the capability to measure customer experience, it is considered inferior from a data-set perspective to revenue. Where revenue tells you what you achieved, behavioural analytics, however, can tell you *why*, and, more importantly, *where you can do better.*

The future of your business is getting rid of the friction and aligning your customers' behaviour with the brand response. The better you link to consumer behaviour, the more likely I will seamlessly engage with you, as and when I need the utility of a financial institution in my life.

Keywords: Customer Experience, Behaviour, Channel Silo, Inertia, Organisation Structure, Product, Innovation

Endnotes

1 These estimates are extrapolated from customer behaviour trends in retail banking multichannel utilisation, based on data from leading retail banks, monetise and mFoundry mobile application platform providers, NCR, and from research from Aité Group, Forrester Research, Gartner, American Bankers Association and Optirate.

2 Key Performance Indicators "are commonly used by an organisation to evaluate its success or the success of a particular activity in which it is engaged"—Wikipedia

3 Customer Service Representative

4 David Bell, Australian Bankers Association, quoted in *ABC's* 7:30 Report

5 As reported in the *South China Morning Post*, 22 February 2007

6 See MoveYourMoney.info

7 See https://www.facebook.com/Nov.Fifth

8 The Durbin Amendment (Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010) reduced fee income for banks of credit and debit card swipes at the point of sale in the US

9 Credit Union National Association (http://www.cuna.org/newsnow/11/system110311-5.html)

10 Research from Global Reviews and Google Finance, 2010

11 Search Engine Optimisation is a field of research and applied technology that results in websites being optimised for improved search engine ranking against specific keywords, enabling customers to find the intended websites faster and easier.

12 The Boston Consulting Group estimates that the U.S. banking industry will lose $25 billion in annual fee income as a result of regulatory changes that include the Credit Card Act of 2009, restrictions on overdraft fees in Regulation E, and the Durbin Amendment, which aims to cut interchange fees on debit cards

13 Novantas (http://www.novantas.com/retail_banking.php)

14 "Face-to-Face: A €15-20Bn Multichannel Opportunity", April 2011, EFMA/McKinsey & Co

15 UserStrategy customer-facing surveys for Standard Chartered and HSBC across 45 countries over four years

16 Exchange-traded funds

17 See ABA research on e-statement usage cost benefit statistics (http://www.aba.com/Members/Research/Documents/a1d7d123032b46eeb48cd428e8ca9b6fGreenBanking.pdf)

18 North American Technographics Financial Services Online Survey—Forrester Research Q2, 2008

19 Optirate and Andera Research—http://bankblog.optirate.com/how-much-do-you-spend-on-customer-acquisition-are-you-sure/#axzz22QFcHE7i

20 "The ROI of Usability", Usability in the Real World—Usability Professionals Association (www.upassoc.org)