

Opportunities for Action in Financial Services

IT Simplification in Financial Services

THE BOSTON CONSULTING GROUP



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Over many years, the IT function in financial institutions has evolved from a mere transactional tool into a pervasive, integral element of virtually every aspect of doing business. This transformation has constituted a fundamental, structural change in the financial services arena and has put IT performance at the top of the CEO's agenda at most banks and insurance companies.

Yet most institutions are facing a major IT problem: how to cope with growing complexity. This complexity can stem from numerous sources, such as funding models that make it difficult to pursue long-term, low-ROI projects like IT application consolidation; short-term business decisions whose cumulative IT ramifications become problematic over time; old and inefficient legacy systems that are never retired; numerous new applications that are incrementally patched in without sufficient regard to their effect on the long-term IT environment; and poor integration of IT systems following mergers and acquisitions.

As it evolves, IT complexity causes severe problems for financial institutions and their customers alike. For example, employees often see only a portion of any given process and are unable to get an integrated picture of a customer's current holdings or position on one screen. Staff must deal with multiple applications that show inconsistent or incorrect data and must log on to numerous systems every day. Customers, for their part, must cope with the staff inefficiency that results from a disjointed IT landscape and frequently must turn to multiple channels to resolve issues—often with different points of access providing conflicting information.

Moreover, from a cost standpoint, IT costs are growing faster than any other category for most financial institutions. And between 60 and 80 percent of IT budgets usually go toward maintenance, with about half of what remains being committed to wiring in new applications. Precious little is left over for investment and renewal. Indeed, in a value-creation sense, the cost of IT's effect on staff productivity and morale is greater than the cost of capital for most banks.

The problems stemming from IT complexity can often be solved by radically simplifying the IT landscape. Such an initiative can also reduce overall IT costs by up to 30 percent and provide significant benefits in terms of increased flexibility in implementing future changes to the IT environment. But how can banks go about a comprehensive IT streamlining?

Taking Stock and Taking Action

A critical first step in simplifying IT systems is to diagnose the current IT environment. This is an onerous task in itself, given that many financial institutions have put layer upon layer of systems and infrastructure into their organizations through continuous enhancements and occasional large projects. In addition, fundamental design changes have forced some institutions to use their IT systems in ways that exceed the intended capacity. For example, single-product systems have been stretched to handle multiple products, single-channel applications (such as branch-based ones) have been extended to cover multiple channels, and batch-based systems have been “upgraded” to support real-time transactions.

To initiate this diagnostic phase across all layers of the IT architecture, companies must determine the exact

number and functionality of applications, interfaces, data repositories, and technical infrastructure elements—as well as their age, size, and long-term fitness and compatibility. They must actively search out application overlaps and gaps in business-process support. And they must thoroughly explore drivers of costs and how costs are allocated.

The second step is to define the *target* IT landscape. Where do you want your landscape to be when the simplification process is complete? In this phase, it is critical to identify long-term business objectives and to align your target IT landscape with these goals.

The third step is to develop a series of programs to attack IT complexity aggressively. For example, multiple, inconsistent data sources must be streamlined into a single, comprehensive source. The frequent hodgepodge of duplicated, overlapping applications (which often includes functional gaps) must be honed into a well-aligned, flexible, responsive, lean force of applications. Interfaces must be transformed from a system of redundant, point-to-point links that share no standard to a network of core, distinct interfaces that have a common standard. And overall IT infrastructure must evolve from a design of multiple platforms with excess islands of capacity (and a lack of scale) to one of consolidated platforms that are fully utilized and able to exploit both scale potential and the opportunities presented by new technologies as they are developed.

In parallel with the above steps, financial institutions should try to weed out underperforming products that add to IT complexity; streamline business processes (by eliminating redundant tasks, for example); and bolster human resources by filling gaps in skills and raising accountability. The ultimate goal is to significantly simplify and streamline the overall IT

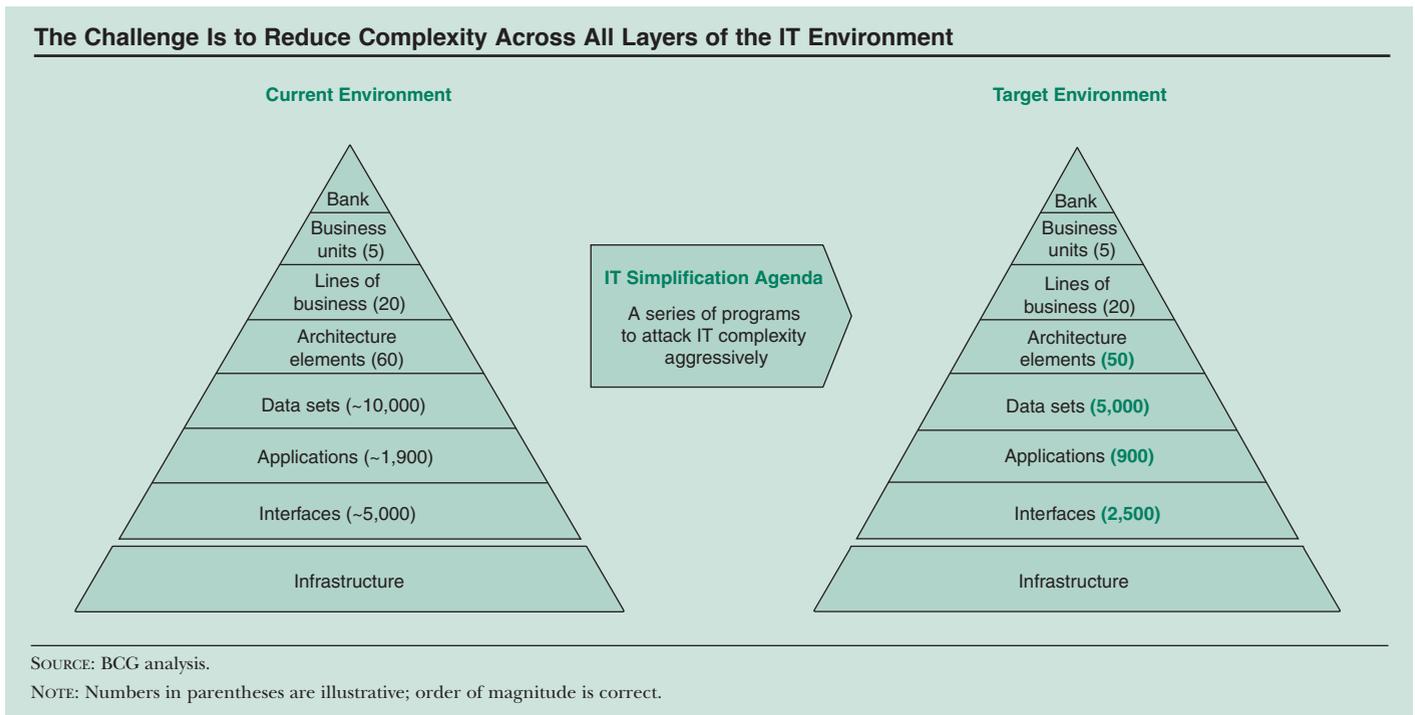
environment and to achieve a high level of IT commonality. (See the exhibit below.)

There is another important dimension to IT simplification that must be addressed along with the nuts-and-bolts steps discussed above: organizational structure. The fact is that organizational boundaries often exacerbate IT complexity issues and make solving them more challenging. Regional branches, business units, and other entities often have their own IT investment priorities and decision-making processes that can work at cross-purposes. A critical step in overall IT simplification, therefore, is to revisit the organizational and governance structures that contributed to the evolution of IT complexity in the first place.

Accordingly, a target IT landscape should be combined with a target IT organizational structure that will foster a high degree of long-term IT efficiency and simplicity.

Less Is More

Although the majority of banks are still struggling to battle IT complexity, a few institutions have taken the offensive with considerable success. For example, one European bank, through a series of carefully planned and executed acquisitions, managed not only to avoid adding to IT complexity but also to consolidate its product systems and achieve a lead-



ing cost position in IT. Similarly, one Chinese bank used an opportunity presented by entering a new market segment to replace, modernize, and simplify its IT landscape.

Business initiatives concerning areas such as product innovation, operational efficiency, and customer service can also provide the impetus to simplify IT. One Australian institution, through a drive to improve customer service, dramatically reduced its number of assisted and self-service applications, and improved the integration of information about customers, accounts, process performance, and staff. Another Australian company, prompted by several business initiatives plus a keen desire to manage IT better, has over the past seven years reduced its 6 core product systems to 2, its 12 IT networks to 1, and its 8 computer platforms to 3. There is also the case of a major U.S. bank that is currently in the process of reducing its number of desktop applications from 415 to 40.

Whatever the immediate catalyst for IT simplification projects may be, it is crucial to set clear objectives. In one major IT simplification in which we were involved, the goals were

- to rationalize and consolidate product-administration systems
- to replace, integrate, and decommission assisted and self-service applications
- to further integrate information across the enterprise about accounts, customers, staff, and process performance
- to consolidate and establish imaging, document-management, and workflow systems

After a thorough diagnostic phase and careful planning of the target IT landscape and organizational structure, a program of nine overall initiatives was undertaken to reduce IT complexity along the above lines. Virtually all product areas were affected, including core retail-banking products, managed investments, life insurance, personal loans, and credit cards. More than 300 major applications and many minor ones came into play, each of which was scrupulously evaluated for long-term effectiveness, user friendliness, flexibility, compatibility, and value in achieving core business objectives. The project is still ongoing, but of the principle applications in question, a total of 70 major applications (and many related minor ones) are being either retired or decommissioned. In fact, these and other streamlining initiatives have helped the bank retire nearly 25 percent of the key IT applications in its overall portfolio within one and a half years. The related productivity improvements and cost reductions have been significant.

Now's the Time

Many years ago, IT was strictly a back-office affair. Then it grew into a front-office matter as well. Today IT has become the critical tool that links the front and back offices of financial institutions—both with one another and with customers through such avenues as PCs, mobile phones, and ATMs. But many institutions have not exploited the potential benefits of this interconnectivity because they have tied their own hands by building multiple systems on top of one another, with many interfaces, and have tried to manage disparate, unreconciled data repositories.

But the handwriting is on the wall. Information technology will only become more important to overall performance and profitability in financial services in

the future. That's why IT simplification is important *now*. Indeed, many financial institutions are trying to embark on more modular, partly service-based architectures. But if in that process they do not clean up their current IT landscapes, these companies will only add another layer over their present systems and may squander their investments in new ones.

It should also be noted that IT simplification is a top agenda item for CEOs not just in financial services but in many other industries as well. General Motors, for example, has reduced the number of its mission-critical applications from 7,000 in 1996 to 3,500 today, with the simplification contributing to annual savings of \$1 billion. IBM has slashed its IT expenditures by 30 percent over the past ten years by simplifying applications and infrastructure. 3M Corporation plans to reduce applications by a factor of five. There are many more examples.

Of course, IT simplification projects are not without risks. They take time and resources, both financial and human. Also, for example, discussions about exactly which applications and which underperforming IT-complex products should be eliminated can be long and difficult because different factions within each institution may have different stakes and preferences. Debates can turn contentious at times.

But banks, insurance companies, and other financial institutions owe it to themselves to overcome these potential hurdles. The benefits of effective IT simplification can far outweigh the amount of resources required to achieve the goals. When IT simplification is executed successfully, it fosters customer service that is more responsive, reliable, and convenient. It cultivates fully engaged staff people who are both motivated and empowered to achieve results. It leads to simple processes that are fast, accurate, and efficient.

In addition, IT simplification should not be just a one-off exercise but an ongoing process. An organizational structure should be put in place that ensures such vigilance. Finally, the cost ramifications of IT simplification are enormous. According to some estimates, IT complexity is costing firms worldwide \$750 billion per year because of lost productivity when systems are cumbersome to use, inefficient, or “down” altogether.

Financial institutions that act decisively to reduce IT complexity—and that go about it in the right way—will gain considerable competitive advantage as a result. Can your firm allow itself to be left behind?

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