

Lean Advantage in Banking

Bringing Together IT and Operations to Deliver Customer Value

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Given the current turbulent times, it has become imperative for many firms in the financial sector to undertake drastic transformations. Now, more than ever, technology has become an important means of helping banks to “reinvent” themselves with regard to both cost efficiency and revenue generation. Of course, sustainable transformation requires a close alignment among strategy, operations, and IT. But technology can be the linchpin of meaningful strategic and operational change.

Technology is enabling aggressive cost efficiencies through integrated IT support of comprehensive products on a global scope—incorporating process automation that brings lower transaction costs and greater price transparency, as well as boosting scale and reducing complexity across the value chain. Revenue generation can be significantly enhanced when technology is designed to support the multichannel and cross-enterprise strategies that are so critical to product origination and servicing. Technology also plays a key role in developing superior tools and analytics to reinforce comprehensive risk-management techniques, which are essential to a successful bank strategy.

So how can banks deploy technology in a way that enables a long-term, sustainable transformation? The Boston Consulting Group’s *lean advantage* approach can help in developing a technology plan that is tightly aligned with an overall transformational strategy. Our approach takes an end-to-end perspective of bank operations and applies “lean” principles to enable the optimization of processes that enhance the customer experience through seamless interaction and servicing across the bank. It focuses on activities that create

customer value and that simultaneously achieve “intelligent” cost optimization. Because operating costs at typical U.S. banks represent as much as 60 percent of noninterest expense, the redesign of operations is fundamental to remaking the business. Our approach has helped banks around the world realize impressive efficiency improvements (15 to 20 percent cost savings) along with solid gains in customer satisfaction and loyalty as well as enhanced risk-management metrics, leading to strong revenue increases.

What Is “Lean Advantage” in Banking?

Lean advantage is a unique approach that incorporates a set of broad-based tools to transform banking operations. It looks at operations holistically and seeks opportunities to improve end-to-end processes and build strategic advantage by instilling organizational and cultural change—following the example set in the 1970s by Toyota, which first embraced the “lean” concept that operations are a strategic asset to be leveraged rather than merely a cost to be managed. As applied by BCG, the approach draws on the best ideas of top-down operations transformation—as well as the more inclusive, bottom-up lean and Six Sigma techniques—and adapts them to a banking context.

Any transformation is done at a cell level (that is, a business unit, function, or service channel, depending on the objective) to ensure that change occurs systematically and in manageable terms. Lean advantage takes the best tools from lean strategies—such as value-stream mapping—and supplements them with the innovative use of IT to improve operations. As a result, it explores opportunities, such as outsourcing, that conventional programs often overlook and

goes beyond just back-office costs to ensure that the full benefits of transformation are identified and implemented.¹

What we call *customer centricity* is the overarching driver of a lean transformation in banking. (See Exhibit 1.) A robust customer strategy requires a complete understanding of the customer relationship in order to develop the integrated information elements that enable differentiated customer experiences while also eliminating unnecessary complexity from customer interactions. Defining the optimal customer experience and understanding the sources of customer value can help to determine the guiding philosophy of the lean transformation program on both the cost side and the revenue side. The operational strategy that best addresses customer expectations is then enabled by technology.

The strong implication is that operations and technology are core components of a bank's overall business strategy. Viewing operations strategically will translate into measurable results—lower costs, higher revenues, and improved customer satisfaction. More often than not, the

factors that drive customer value also drive these priorities. With a clear understanding of customer expectations, lean advantage reviews the existing operating model as a whole, rather than in disconnected parts. By seeking ways to improve end-to-end processes that create strategic advantage, lean advantage generates outcomes that are much deeper and longer lasting than the results of conventional operations-improvement programs. Success is gauged not by the sum of one-off cost improvements but by the overall profitability generated through fundamental transformation.

With lean advantage, we carefully evaluate and refine the operating model on two key dimensions. (See Exhibit 2.) The *business architecture* defines how operations are configured and addresses questions such as the extent and nature of consolidation and specialization, the location and flow of processes, the degree of outsourcing, and the application of technology. The *organization model*, which describes how the business

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1. For a more complete discussion, see "Banking on Lean Advantage," BCG Opportunities for Action in Financial Services, January 2008.

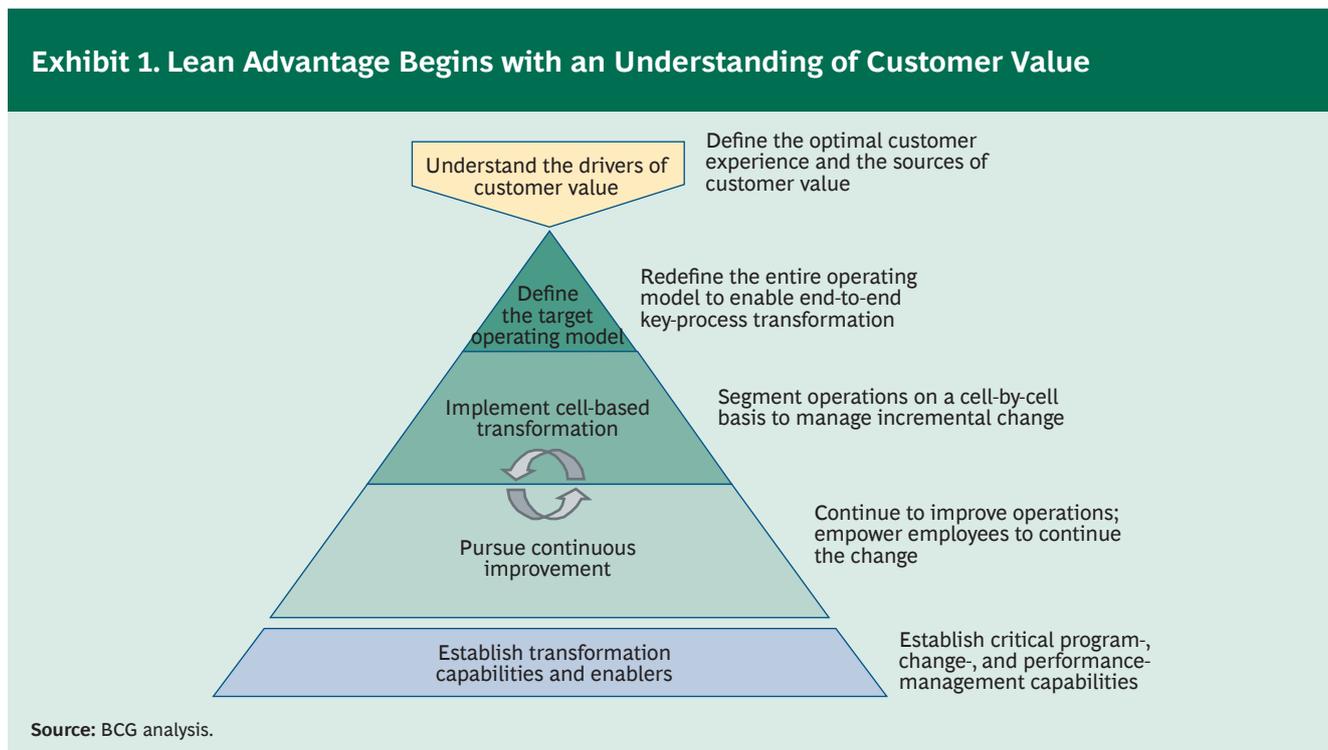
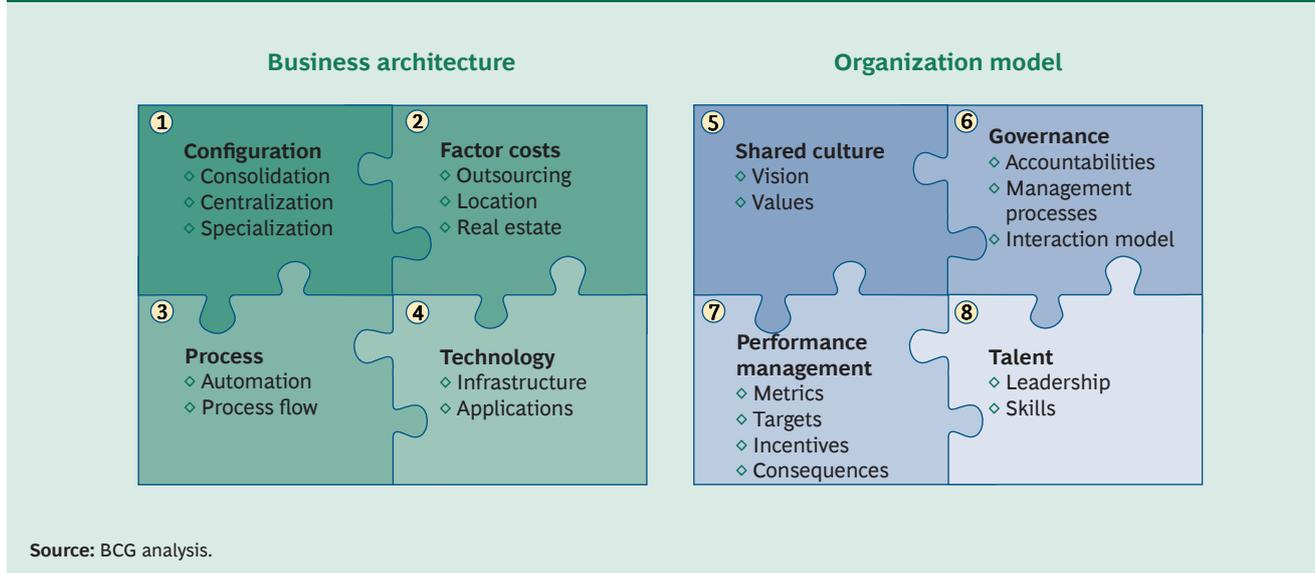


Exhibit 2. Lean Advantage Examines Operations on Two Major Dimensions



is actually run, focuses on core issues such as culture, governance, performance management, and talent—thus cutting across business cycles. Regardless of whether a bank is seeking cost reduction or growth, it must not underestimate the importance of the organizational side of transformation, which is often ignored in operations improvement programs. This underscores the unique nature of a lean-advantage transformation—it is fundamental and holistic, rather than opportunistic and compartmentalized.

Lean advantage places a premium on building capabilities to ensure continuous improvement. It “trains the trainer” and establishes replicable tools and processes that will help the organization sustain a culture in which operations are always seen as a source of strategic advantage. Only by embedding a culture of continuous improvement—which includes training a cadre of lean experts and providing the governance and performance management systems to track change—can banks realize the full benefits of a lean-advantage strategy. In particular, the bank must use technology to put metrics in place that allow its executives to track the delivery and longevity of operations improvement. This focus on continuous improvement enabled one of our clients to achieve additional savings of 3 to 4 percent annually over the four years following the initial transformation of its operations.

The Linkages Between Operations and IT Within Lean Advantage in Banking

What translates customer expectations into reality? First and foremost, it is a tight alignment between bank operations and IT. While the target operating model redefines the processes, it is technology that turns that vision into reality. Customers rarely think about operations. Yet operations, more than any other factor, will influence how a customer feels about a bank. Customers define their banking experiences by personal experience: How fast did the bank respond to my request, approve my loan, or execute my transaction? Banks rate themselves by measuring customer advocacy and “churn,” both of which reflect a customer’s feelings about the bank in very clear positive or negative terms.

Any operational model driven by customer expectations requires solutions that are geared toward value-adding services. For retail banks, the branch as a service channel is making a comeback as a significant means of revenue generation. Origination and servicing driven by a stronger focus on customer satisfaction and retention—often through multichannel strategies—are critical to revenue growth. Customers want to be supported by channels accessible from multiple phone and computing devices, making it important for banks to ensure service functionality and process consistency across channels.

By the same token, providing full customer access across all products (including credit cards, loans, and mortgages) through a single access point is equally important. This is leading to stronger pricing personalization, a push for product bundling, and a stronger focus on product innovation. Branch and operations integration and automation are becoming a core investment area. To reduce the operational costs of both sales and service, banks are looking to standardize and automate processes across channels to provide consistency to customers, as well as to drive operational best practices across the enterprise and to consolidate support functions where applicable. This requires a lean *technology* strategy—less complex but also very robust.

It is important to note that lean advantage does not downplay cost savings: indeed, cost reduction is a priority of most operations programs, and especially so given the current market environment and its challenges to the top line. But it provides a means of balancing cost savings against potential revenue gains. Other banks have used lean advantage to boost customer satisfaction and loyalty by as much as ten percentage points and increase revenues by 5 to 10 percent.

Talking to a bank’s customers and executives and studying its data—for example, its inventory of customer complaints or surveys—can help pinpoint where better operations will have a multiplier effect on profitability. This is accomplished in a lean-advantage program by using technology to tap into information that already exists in an organization’s marketing databases, operational information, transaction records, and complaint resolution files. For example, in a large North American retail bank that pursued a program to improve its customer experience, we identified six “customer value” themes that could significantly enhance the bank’s ability to radically transform the customer experience:

- ◇ Improved customer-account opening and on-boarding
- ◇ Enhanced customer retention
- ◇ Broader cross-sell processes to bring the full suite of bank products to every customer
- ◇ A seamless transaction experience across businesses and channels

- ◇ Ongoing efforts to revamp lending processes
- ◇ Streamlined new-product and deal-approval processes

Needless to say, these themes were primarily addressed through technology that enabled a common view of the customer, effective enterprisewide coordination (such as referrals and cross-selling), and straight-through processing for all transactions. (See the sidebar “Lean Advantage in Action.”)

Lean Advantage in Action

The customer experience is dependent on how closely the technology supports key processes. Recently, customers of a large North American bank were becoming increasingly frustrated with service quality. On the retail side, prospective customers were lured into the bank’s branches by an advertising campaign that promised to make banking easy and friendly. Instead, they encountered a daunting and complex process: antiquated paper-based forms to fill in, high error rates in processing new accounts, difficulty in transferring funds from their old bank to the new bank, and confusion about the different products and services. On the corporate side, things weren’t much better. Commercial loan applications were also paper based, turnaround times were lengthy, and there was an 80 percent error rate in processing. Many customers decided to go elsewhere, and the bank’s financial performance and market share suffered as a result.

The bank brought in BCG to help reconfigure its operations in order to regain customer confidence and market share. Using its lean-advantage approach, BCG launched a series of programs to dramatically improve the customer experience. A combination of radically optimized operations and upgraded technology that enabled electronic data capture, automated decisioning, and channel-agnostic processing leading to point-of-sale fulfillment has, in just 12 months, put the bank on a path toward volume increases that will add between \$300 million and \$400 million in top-line dollars in just its first phase over three years. Understanding the connection between operations and the customer experience is essential to transforming operations into a strategic asset—and technology is the key to a successful transformation.

For another large North American bank, one that has more than 2,000 branches and 10 million customers, we found that decreasing the turnaround time for a mortgage application would produce revenue gains five times greater than the savings that could be squeezed out of mortgage operations. The key to achieving this was to align all of the functional elements of the value chain around a common vision—the 15-minute mortgage. Each “member” of the value chain agreed to contribute some significant change in order to deliver a truly transformed experience for the customer. Product development, for example, designed a dramatically simplified contract; the various sales channels began to collaborate in qualifying leads, booking appointments, and steering customers to the channel that best suited their needs; and the fulfillment team worked with the channels to enable a streamlined central-fulfillment capability.

All this was supported by IT, which delivered enhancements to existing risk-management and other capabilities as well as new imaging and workflow functionality, allowing the bank to orchestrate the value chain and provide transparency. The end result was a dramatically simplified customer experience, with most customers able to get an answer from the bank in their first interaction, regardless of channel, and to completely fulfill all of the requirements in only one or two branch visits.

The Role of IT as a Catalyst for Lean Advantage

Because a lean transformation is a cross-enterprise effort, IT plays a pivotal role in ensuring that logical linkages are established and that technology efforts are not reinvented for every business unit. From its cross-enterprise vantage point, IT has the ability to shine a spotlight on places where significant improvement can be made. Whether for access to vital and timely information or for automating processes, IT is the catalyst for the makeover of banking operations. For its part, IT has successfully begun to remake its image within the bank by offering technology-based options that simplify and elevate the customer experience.

It is important to ensure that the operating model—at a high level—aligns with the drivers of customer value. Reviewing the model against these drivers will

highlight major changes required in end-to-end processes. IT is critical in areas of customer service delivery. IT also plays a key role in providing simple dashboard tools for tracking performance. This helps ensure that the bank’s focus is on sustained delivery while undergoing continuous transformation.

Lean techniques can transform and leverage operations as a competitive differentiator.

In the end, financial institutions, especially banks, can learn valuable lessons from the experiences of industrial companies that have successfully transformed themselves by treating operations as a strategic asset.

Lean techniques can transform and leverage operations as a competitive differentiator. There is little doubt that embracing a lean-based technology strategy can help banks be “cost smart” and at the same time increase revenue by focusing on what matters most to the customer. Be it front-end, middle-office, or back-office processing, leveraging technology and adapting the underlying organizational and governance processes to ensure continuous improvement are the key elements of a smooth, seamless, and efficient operational strategy—which drives a bank’s bottom line.

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