WHITE
PAPER

Outpace the Competition

Build a HyperConnected Bank.

Transform Retail Banking at the Branch

LUMEN℠

Banks Must Transform to Survive

Retail banks are under unprecedented competitive pressure. After decades of steady growth, consolidation, and branch network expansion, technological and regulatory changes are disrupting business as usual. New market entrants and revenue disintermediation are coming from traditional retailers, and from new competitors in FinTech. At the same time, customers have become increasingly comfortable with technology, which has driven their demand for superior service and convenience — and drastically changed their banking habits.

While this new business environment impacts every part of a banks' operations, retail branches are ground zero for change. Branch network expansion continued in the U.S. up until 2009. Today, banks are closing or repurposing/rightsizing branches in response to widespread trends, including a slowdown of branch-generated revenue growth, widespread adoption of digital channels, changing customer demographics, and increased omnichannel banking.

Contents

Challenge

Competitive pressure and client demands require retail banks to transform their branch networks and delivery channels. However, cost controls and resource constraints can limit their ability to implement the IT operating model necessary to innovate and achieve their desired objectives.

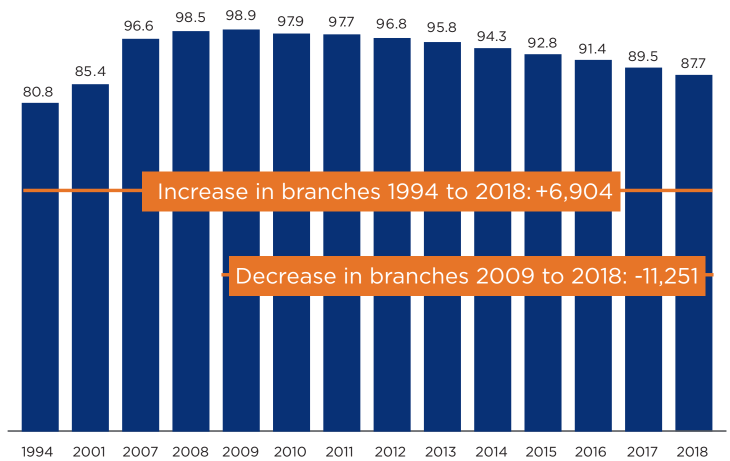
At Stake

Inability to deliver an improved and consistent customer experience will lead to loss of market share and dwindling margins.

Solution

Reduce the risk of costly in-house IT infrastructure transformation by partnering with an experienced Infrastructure as a Service (IaaS) provider

No. Retail Branches in the U.S. (000's)



Source: MarketForce 2019 The Financial Brand

McKinsey Reports: How Banks Improve Efficiency Ratios

Migrating transactions to digital channels, transforming physical distribution networks, and revamping go-to-market strategies can significantly improve a bank's efficiency ratios — by up to 7 percent. Two of the biggest contributors: introducing new branch formats and thinning the branch network, for cost savings of almost 8 percent and increased revenue opportunity of 1.5 percent.1

Nevertheless, despite the high cost of keeping branches open and the rise of less expensive delivery channels, it is too soon to declare the branch irrelevant. Even mobile customers still interact with branches.

> "Despite such systemic changes, branches remain an essential part of a banks' operations and customer-advisory functions. Brick and mortar locations are still one of the leading sales channels. Even in digitally advanced European nations, between 30 and 60 percent of customers prefer doing at least some of their banking at branches."[2]

While mobile banking applications continue to improve, according to a survey by Novantas, "60 percent of Americans would still rather open a new checking account in person at a bank branch than on a phone, tablet or desktop computer."3 Banks have yet to maximize the potential of other channels, so retail branches remain their strongest strategy for new customer acquisition, sale of complex products, and face-to-face advice and guidance for customers.

Though bank executives recognize that branches are important, they have not developed the most effective branch strategy to keep pace with today's retail customer. Industry experts acknowledge that in order to deliver its full value, a branch needs to be part of a fully integrated customer experience. In a recent survey by research firm Celent regarding retail banking technology, a majority of North American financial institutions prioritized branch channel transformation over "hot" areas such as artificial intelligence, open APIs and core systems replacement.

Banks will not become profitable just by trimming the branch footprint or cutting costs. They need to adopt more agile and modern IT infrastructure to boost branch profitability and ROI. Otherwise, banks will experience a collapse of margins and customer base. Smart transformation requires that banks:

- Understand customer needs and implement omnichannel strategies to deliver an improved and consistent customer experience
- Comply with regulations and remain vigilant in the face of ever-changing and increasing cybersecurity threats, while pushing innovative services and IT infrastructure out to the edge
- Formulate and execute the lowest cost, highest return strategies for serving customers and achieving growth

Understand What Customers Want — and Deliver It

To guide branch transformation, business and IT decision makers need to quickly deliver the services that customers now want. The objective remains the same: increase customer retention and grow revenues. But today's customers have higher service expectations and lower customer loyalty than ever before, so banks need to provide convenience and value or customers will move on.

Bank channels must be integrated and offer the customer self-service, anytime, anywhere, across all banking platforms. This includes online, call center, ATM networks and in the branch.

Today, in order to increase revenue, customer base, and customer loyalty, banks need to exceed expectations and delight their customers. They need to analyze and understand individual needs, usage, and preferences, and differentiate themselves by consistently offering more personalized service than their competition. Increasingly, personalized loyalty programs are viewed as an important tool to drive revenue and reduce customer acquisition costs.

Robust data analytics platforms, supported by an agile IT infrastructure, enable banks to analyze and manage customer touch points across online and mobile apps, call centers, ATMs, and physical branches, and then use this data to gain insights into customer needs and values. Banks can then leverage these insights to provide more personalized, timely, and innovative banking services, such as reward programs, special offers, and purchase analysis to drive growth and encourage retention. To cross-sell to an existing base more effectively, banks need the analytic capability to go beyond segmenting customers by traditional demographics, and instead must analyze each customer's financial lifecycle, spending patterns, banking channel behavior, and banking product usage.

According to the 2020 Foresight Report on Retail Bank Loyalty Programs, such analytics enable banks to, "target and isolate the most profitable customers and phase out the programs that do not offer significant value to a bank's overall business. Moreover, analytics are enabling banks to provide location-based, real-time discounts in collaboration with merchants. The successful implementation of analytic-based reward programs has become a key differentiating factor for banks."[4]

Ensure Compliance with Regulations

It's not glamorous, but regulatory compliance is essential. In transforming the branch structure, banks need technology that makes it easy to operate within the FFIEC reporting framework and meet all of the requirements for the industries and countries in which they operate. From the head office to the data center to the branch teller, banks have to ensure compliance with an "alphabet soup" of standards and regulations, including the Payment Card Industry (PCI), the Federal Information Security Management Act (FISMA), SSAE 16 SOC 1 and SOC 2 compliance, and others.

Ensuring full compliance is complicated. Banks often turn to vendors with compliance expertise in the myriad of requirements across branch networks.

Deliver Excellence for Less

As the costs of complying with ever-changing regulations increase and revenues stagnate, banks are under pressure to significantly cut their spending. The cost base of many banks is too high to remain competitive. Retail branches must cut costs and generate more revenue to justify the expense of owning and operating them. Banks may need to trim back branches and will certainly have to maximize their traditional strengths — their ability to bring in new customers, facilitate sales of complex products, and offer face-to-face advice and guidance to customers.

Many banks prioritize cross-selling to existing customers and building customer loyalty over reducing branch service costs. To encourage customers to use the branch as an integrated and personalized channel, retail banks need to make changes in their culture, technology, and configuration of traditional branches.

Changing culture can be as easy as conducting retail branch personnel training to prioritize relationship building over traditional transactions. New technologies that improve staff productivity and aggregate and report data from various customer interactions with different channels may support this shift. But the most dramatic change is likely to come from optimizing configuration of network branches. As customer foot traffic continues to decline, banks have to redefine their traditional understanding of what a branch is. For example, some smaller branches are becoming little more than self-service, unstaffed kiosks, while larger city branches transform into full-service flagship branches.

As a result, it is likely that branches will employ fewer staff, but will leverage additional technology tools. IT transformation extends far beyond visible signs of change, such as roaming bank staff carrying tablets on site. As part of cost-effective branch rightsizing, banks need to remotely self-provision network configurations without deploying IT people at the branch. As banks continue to push services out to the edge, they must reduce the massive support burden, alleviate the potential for security breaches, and initiate a more advanced network for innovative branch service rollout.

Don’t Let the Network Become a Chokehold on Branch Services

The network is a strategic opportunity for branch transformation projects. Branches need high-speed network access to deliver new services, handle multiple platforms and capture transactions securely. Branch transformation requires a long-term plan for secure, advanced network capabilities. Banks may also have performance, functionality, and capacity restrictions with existing networks. It may be more difficult to secure networks across different vendors. A responsive network will enable advanced banking services along with cost efficiency.

Think Outside the Data Center Box: Outsource IT Infrastructure Services

Banks must implement an agile IT infrastructure that supports a seamless customer experience, using lower cost channels for transactional flow and higher value channels for premium clients. While IT professionals may initially view IT transformation as a cost savings exercise, the long-term benefits include efficiencies in IT and business operations, enhanced corporate agility and increased profitability.

For a Fully Integrated Infrastructure, Choose Just One IT Partner

The transformation of in-house IT infrastructure has traditionally been a complex undertaking, with a great deal of implementation risk and capital outlay. It ultimately creates a new legacy system that will require an update, usually sooner than expected.

To break free of this cycle and reduce the risk and cost of transforming in-house IT infrastructure, banks can outsource to an Infrastructure as a Service (IaaS) provider. Outsourcing makes sense from financial, IT operations, and business standpoints.

Financially, banks can fund their new infrastructure from an OpEx rather than a CapEx model, which supports capital adequacy and liquidity ratios and improves their efficiency ratios.

From an IT perspective, outsourcing increases efficiencies by consolidating management of networks, data operations, and branch computing power to remove complexity from both transformation and ongoing operations. An IaaS provider also offers broad and deep industry expertise. Branch transformation projects require a specific set of skills across networks, computing, and security services, but too often banks incur risk and inefficiencies. They are fragmented across network providers, computing suppliers, software vendors, and infrastructure services. But with an expert infrastructure partner, banks can tap into a large pool of diversified expertise around the latest technologies and best practices while capturing efficiencies and reducing operational costs.

Most importantly, from a business point of view, outsourcing allows banks to provide flexible branch capabilities at lower cost points, without needing IT staff at the branch. A centralized, outsourced IT infrastructure can support a range of branch configurations from a self-service kiosk to a fully staffed flagship branch, offering agility to support the most demanding retail customer. By leveraging hybrid IT and IaaS models, bank branches can provide a wide range of services — such as colocation, managed hosting, cloud, network, and consulting — to meet both current and future business needs and customer demands. Outsourcing enables banks to move at their own pace to access the expertise, tools, and capacity they need to meet their goals — whether those are for branch transformation, extension to new digital channels, or other operating efficiency improvements.

The fastest and most effective way for banks to implement and scale new services, products, and capabilities is through IT infrastructure outsourcing. To transform retail branch capabilities and align their cost structure with the new economics of retail banking, banks should look for an IT partner that understands the banking industry, the challenges banks face, and new and ever-changing regulatory requirements. In addition, banks should avoid piecemeal outsourcing. To simplify the transition process and maximize cost efficiency, IT effectiveness, and business agility, banks should look to build a comprehensive partnership with one IaaS provider that can do it all — delivering a unified managed services approach across voice, data networks, computing, infrastructure, and security services.

Footnotes

1. McKinsey & Company, The Future of U.S. Retail-Banking Distribution, Aug. 2014.
2. 'A bank branch for the digital age', McKinsey & Company, July 2018
3. 2020 Foresight Report: Retail Bank Loyalty Programs, July 2018
4. Novantas, Americans prefer bank branches over mobile apps for opening new accounts, Feb. 2018.

About Lumen

Lumen (NYSE: CTL) is the second largest U.S. communications provider to global enterprise customers. With customers in more than 60 countries and an intense focus on the customer experience, Lumen strives to be the world's best networking company by solving customers' increased demand for reliable and secure connections. We also serve as your trusted partner, helping you manage increased network and IT complexity and providing managed network and cyber security solutions that help protect your business.

To support our banking clients with state-of-the-art IT and competitive cost advantage, Lumen offers an audit-ready FFIEC reporting framework, data modeling and analytics practices, a consolidated managed services model, and huge economies of scale.

Our broad networking portfolio gives you the ability to deliver electronic services from T1s to 100G networks. And, we take care of project implementation, including a road map from voice to data to video.

For more information about Lumen services, please visit lumen.com