Reducing Complexity in Retail Banking: Simple Wins Every Time

Banks offer a dizzying array of products and services. Add to the mix new regulations and shifting customer needs, and the industry becomes even more complex. One key to success: a streamlined product portfolio.
Like houses with attics full of worn-out armchairs and discarded tables hidden above newly decorated living rooms, most banks have a stockpile of overhauled, outdated products tucked away behind a few shiny innovations. Many of these products require complex activities but have nothing to do with new sales. And the glut of products is limiting not only profits but also the flexibility to react to external pressures.

It is time to clean out the attic and focus on products and features that your customers not only want but are willing to pay for. Gaining a competitive edge requires tackling the product complexity challenge (see figure 1).

A Complex Portfolio Cuts into Profits

Today’s bank customer wants a variety of products and services. Delivering such variety, however, often results in an overly complex product portfolio that can cut significantly into profits. Consider the front office: More products means bank tellers need extra time to explain and process transactions for a variety of products, features, prices, and discounts. Each transaction is likely to have a whole new set of relevant products for tellers to juggle, from cash payments and making deposits to selling investment funds and saving plans and even educating customers about new interest rates for certificates of deposit. This highly complex front office not only frustrates customers who expect flawless treatment, it also drives cost-to-serve up significantly. Our review reveals that 75 percent of processing costs in branch-focused banks comes from the front office; in addition to the higher cost-to-serve, this front-office-centric approach reduces the time available to generate revenues.

Even new sales can cut into profits. When customers can’t clearly see why some products cost more than others, sales advisors often offer discounts as a last resort to meet their demands. These discounts are usually tied to a trial period, but converting trial period prices back to standard prices does not always happen for fear of losing customers.
The middle and back offices also feel the weight of complex product portfolios as they are required to maintain the full portfolio for an undefined period—if a customer with a legacy saving product inquires about a historical transaction, the back office needs to be able to trace and document all related calculations.

In addition, IT costs are impacted by an overly complex portfolio. It is not uncommon for banks to keep certain legacy systems running because they host a large portfolio of legacy loans or long-term mortgages and prefer not to have to contact clients in the event of system migration problems.

The Origins of Bank Complexity

Across the board, complex product portfolios push revenues down and costs up. But how did the banking attic get so cluttered in the first place? Three reasons stand out:

A product-centric view

Traditional banking offerings tend to take a product view rather than a holistic, customer-centric view of an offering, valuing the success of individual products more than the full revenue potential of individual customers. Product managers are encouraged to maximize earnings in their product category without considering the bank’s overall profit and loss. Products that create value and additional complexity are only viewed in terms of the value created and not the complexity caused. For example, a new loan product can create new business but make the application process for other loans more complicated.

No product life cycle

The banking industry is not alone in launching products that sell for a while but then are replaced by other products to entice new customers. Where banks differ is in not systematically discontinuing old products when new ones are added (see figure 2). In consumer goods or software, the idea is to shift customers to the next generation of products while phasing out the old ones. Customers who resist are charged higher service costs.

Figure 2
As new bank products are unveiled, old ones rarely get phased out

Source: A.T. Kearney analysis
It is not unusual for a bank to maintain portfolios with more than 500 products, two-thirds of which are legacy products that do not generate new sales or revenues. One of our clients had more than 15 different savings products, with just three accounting for 90 percent of new product sales. And specialty products amplify the problem. One bank offered a savings product with a variable interest rate that depended on lottery results and for a decade after the promotion ended was still tracking lottery results.

A complex product blueprint

Digging deeper into the core product setup sheds more light on a bank’s complex blueprint. There are hundreds of product variations, mainly the result of mergers, multiple brands, and accumulated legacy products. The situation is exacerbated by a thousand or more specifications in product features, from credit interest rates and preferred payment methods, to technical parameters required for system implementation, and pricing features that describe the algorithms of the fee and interest calculation. And different pricing—from standard fees with special discounts for certain customers or product combinations to negotiated fees for individual clients—make it yet more complicated.

Dig deep. Portfolios can be cut by 30 percent or more without causing significant pain.

Now apply those combinations to processes such as product launch, administration, transactions, and closings, and the complexity becomes even more incalculable. In Brazil, the number of different risk-scoring models is estimated at well above 250 primarily because of the wide range of products. In Germany, some product features were used by no more than 200 customers, but the features still had to be implemented in IT and operations—at a significant cost.

Over time, banks have grown accustomed to these complex product portfolios and the external factors—digital disruptors, regulatory environment, lack of transparency—that further compound the situation (see sidebar: Outside Forces Pressuring Banks to Simplify on page 7).

Smart Simplicity

The perfect storm of internal and external factors is pushing the need for less complexity and simpler product offerings. Our three-step approach can make an immediate impact and help capture growing advantage in the drive to reduce retail bank complexity.

Clean out the attic

Get rid of the old furniture. Analyze products in light of customers, revenues, and costs to identify the showcase pieces and the dust collectors. Evaluate the strategic relevance and regulatory obligation of each product to determine its future need. And then dig deeper: Cleaning out bits and pieces won’t make much of a difference. A portfolio reduction of less than 30 percent is not enough. Depending on the starting point, portfolios can be cut by 30 percent or more without causing significant pain.
Build bank products like the automakers build cars

The product portfolio must become lean and stay lean. We believe the best tool for this is modular product design, a concept that originated when Toyota and other automakers designed components that can be assembled in a variety of ways to meet individual needs. Vehicles are built on the same platform but differentiate on the accessories to capture economies of scale and to meet drivers’ needs (see figure 3). The same principle is being applied to financial products and services. U.S.-based Union Bank, for example, unbundled the traditional checking account and launched Banking By Design to let customers create an account that fits their needs, choosing only the features they want and opting out of those they are not willing to pay for.

Figure 3

Modular products: how to stay lean and capture economies of scale

A modular product offering requires some reengineering to synchronize core features, price calculation algorithms, and processes across products. For example, when and how credit interest rates are calculated must be harmonized across all products. This requires a detailed analysis of as-is and to-be product designs, but it is worth the effort because modular products can have an immediate impact on IT and operations and offer more flexible ways to launch new products.

Life-cycle management supports this new lean framework. When a product is launched, its life cycle is already defined with exit strategies and policies in place via contractual clauses. Pricing fluctuations must also be addressed: Revenues across all product categories can be increased by 5 to 15 percent simply by standardizing pricing policies and giving advisors far less leeway to offer discounts.

When built on the right platform, the portfolio has standard components, a well-defined mix of basic and optional modules, and some customized products for key customers.

Match products with customer preferences

The last step in streamlining the product portfolio is to match products with customer preferences—moving from a product-centric view to a customer-centric view. In Germany,
independent financial advisors MLP and AWD offer customers comprehensive solutions rather than single products, and Total Merrill in the United States offers a broad range of advice about investments, retirement, banking, credit, and lending.

The idea is to take a customer view to generate revenue; this may include free-of-charge basic items such as checking accounts and credit cards, while heftier charges are reserved for less competitive but more valued products such as retirement provisions, mortgages, asset allocation, and other offerings that meet individual customer demands.

While understanding customer preferences is not that difficult—it is often gained through deep financial background information and data on recurring transactions—the trick is converting this knowledge into upselling or cross-selling opportunities. Here, it is useful to take a lesson from retail giants such as Amazon that excel at forecasting the next best product by understanding and internalizing customer demands and predicting how these demands will develop.

The point in time when customers make a purchase decision is also shifting thanks to the ubiquity of online information and interactions (see figure 4). The buy decision takes place long before any face-to-face interaction occurs, so a business model that relies on personal advisory skills will no longer work. Anticipating customers’ preferences and meeting their needs requires a streamlined product portfolio across multiple channels with just the right mix of prices and services. So different products are put at the forefront at different price points for young customers than for senior citizens. Internally, organizational decision making must also shift from a single-product perspective to a customer-centric perspective.

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**Figure 4**

**Bank customers drive product sales**

<table>
<thead>
<tr>
<th>Customer need</th>
<th>Lead generation</th>
<th>Consultation</th>
<th>Purchase</th>
<th>Use</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Past</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Determine product preference</td>
<td>Interact with bank advisor</td>
<td><strong>Product push:</strong> consult with branch sales person</td>
<td>Sign on the dotted line (in person)</td>
<td>Talk to family and close friends about the bank’s performance</td>
</tr>
<tr>
<td><strong>Present</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Product pull:</strong> determine product need by discussing with peers</td>
<td>Perform independent research, comparison shop</td>
<td>Interact personally or via video conference</td>
<td>Close the deal online or on a mobile device</td>
<td>Use social media to broadcast thoughts about bank performance</td>
</tr>
</tbody>
</table>

*Source: A.T. Kearney analysis*
Getting Smart about Complexity

Complex product portfolios are having adverse consequences for the retail banking industry, with new regulations and digital further complicating the situation. A structured and smart approach to complexity can directly improve product profitability. Now is the time to roll up your sleeves and get rid of outdated products, build a framework for the future, and align the portfolio to meet customers’ needs. Reducing complexity will bring both the quick wins and the enduring changes needed to win the race for profits.

Authors

Mathias Ullrich, consultant, Frankfurt
mathias.ullrich@atkearney.com

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