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Branch Efficiency: Today's Cuts vs. Tomorrow's Growth?

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Something's got to give. On the one hand, the physical branch network remains the anchor of most customer relationships in retail banking, both for households and small businesses. And because of this customer connection, the branch will continue to play a prominent role in the future of retail banking.

On other hand, branch networks became heavily overgrown during recent expansion years and now pose an immense expense burden – over half of the total expense base in retail banking – in the wake of the U.S. mortgage crisis and economic slowdown.

How can banks reduce branch expenses without harming the franchise? It is a pivotal question at a time when branch economics are under assault. During the last six years

alone, the total branch count for U.S. commercial banks soared by more than 20%, to roughly 90,000. This far outpaced household expansion, depressing the average number of U.S. households per branch from nearly 1,650 to nearly 1,450.

Underscoring the degree of management conflict on how to respond, some banks are mandating across-the-board branch expense cuts, while others are according veritable kid-glove treatment to their networks, given their pivotal role in deposit formation.

Ultimately, there is an innovative middle path that will allow progressive institutions to achieve transformative changes in branch efficiency. But to get there, banks will need to avoid the temptation to fall back on traditional approaches that, while specific about short-term savings, often overlook new ways to think about markets, customers, services and technologies.

Traditional principles and initiatives used for branch network efficiency enhancement can pose pitfalls in three main areas, including decisions broadly related to: 1) branch locations; 2) branch formats; and 3) branch activities. In all three areas, there is a risk of further embedding current network flaws, limiting the potential for long-term efficiency improvement.

The key is to develop a vision for the future role of the branch network, and then harness short-term efficiency adjustments to help move the network to a much more progressive config-

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