Accelerating Digital Migration: Necessary, Tough and Rewarding

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In the next phase of customer migration from branch to digital, every aspect of face-to-face and voice-to-voice interaction needs to be mapped and evaluated for digitization.

The smart phone era — heralded with the iPhone's launch in 2007 — has accelerated in earnest what prior banking innovations only suggested: true consumer substitution of transaction volumes to electronic channels from the branch. As a result, digital migration is now a key cost reduction lever for banks. Additionally, research indicates that great self-service experiences can enhance customer loyalty by providing convenience, immediacy, and reducing customer effort. But progress on migration is uneven, and the stakes are getting higher, creating a mandate for action in 2017.

The banks that have proactively harnessed this channel substitution trend are gaining ground, taking the lead in slashing branch transaction burdens as more of their customers switch their daily banking activities to mobile/online banking and advanced ATMs. However, it is becoming clear that many others are mired in passive, partial programs, with real implications for future competitiveness.

Many banks have concentrated in a few high-visibility areas (e.g., ATM and mobile deposits), proceeding without a full set of transaction metrics or a formal companywide plan. In the early going, this sparked enough true channel substitution to permit cost-saving reductions in teller staffing across the industry.

Now many U.S. branches are approaching feasible staffing minimums, and resulting staff productivity improvement has slowed. To reach the next level of meeting customer expectations and further improving efficiency banks must go further and automate even more branch services such as softer inquiry or informational services. Simultaneously, they must look at accelerated branch consolidations and closures, which is potentially far more disruptive to customer relationships.

At this point, executives must ask, "Do we have a thorough plan to digitize more of the branch experience as the physical network shrinks? Do we have a plan for originating online the relationships that were otherwise originated in the branches being closed?"

In this more comprehensive phase of digital migration, every aspect of face-to-face and voice-to-voice customer interaction needs to be mapped and evaluated for digitization. And it is not just about economics and technology. Considerations must also include the promotion, education, incentives, and segment tailored approaches that are needed to usher customers and staff through delicate transitions.

Winning banks will pull all of this together in a holistic digital migration program that includes four major components:

- *Measurement.* The bank needs a detailed map of migration rates across all channels for all transactions, service, and sales — not just a few areas, but the total picture.
- *Segmentation.* Channel-based treatments must be tailored for major customer groups, especially remaining heavy users of branch and call center services.
- *Prioritization.* For solid planning, all migratable channel activities must be analyzed and financially quantified, clarifying tradeoffs and potential rates of return on various digital investment options.
- *Execution.* A customer-centered, cross-functional program is needed to assure smooth, appealing transitions and wide consumer acceptance, participation, and

retention as additional layers of digital self-service are rolled out.

THE ROAD AHEAD

Digital migration would be much more manageable in a forgiving setting of high banking profitability. But the current and foreseeable environment is one of pressing conditions and hard choices. Recently hovering at a roughly 9% return on equity, industry profitability is down sharply from a 13.4% average prior to the 2007-08 housing crash.

In turn, banks are eager to reduce branch-related expenses, and staffing in particular, as transactions go digital. Novantas research reveals that over the past five years, the industry has engineered a 20% decline in average teller staffing per branch in full-time equivalents, from 379 FTEs per 100 branches in 2011 down to 302 FTEs per 100 units in 2016 — a roughly 4%-5% decline per year. In contrast, branch counts have come down by a lesser 1%-2% annually during the same period.

Looking out over the next five years, we expect banks will need an additional 20% proportionate staff reduction, plus an equally sharp increase in branch reductions (Figure 1: Mandate for Further Transaction Automation). This sets the realities of minimum branch staffing on a collision course with aggressive productivity assumptions, with the bank stuck in the middle. In fact, our research indicates that teller productivity improvement has hit a period of diminishing returns, with staff reductions out-pacing declines in branch transactions.

The only way out is additional transaction automation that will further lower the branch workload. However, remaining branch transaction volume will be more difficult to migrate (Figure 2: Breaking the Barriers to Further Migration). This challenge is coming at a time when more aggressive branch consolidations and closures will be needed to wring out the overhead associated with obsolete physical capacity.

To be sure, variations on this call to action have been floating around for 20 years, with pundits repeatedly hailing an impending industry inflection point in branch usage that has historically never materialized. But this time around, it appears to be different:

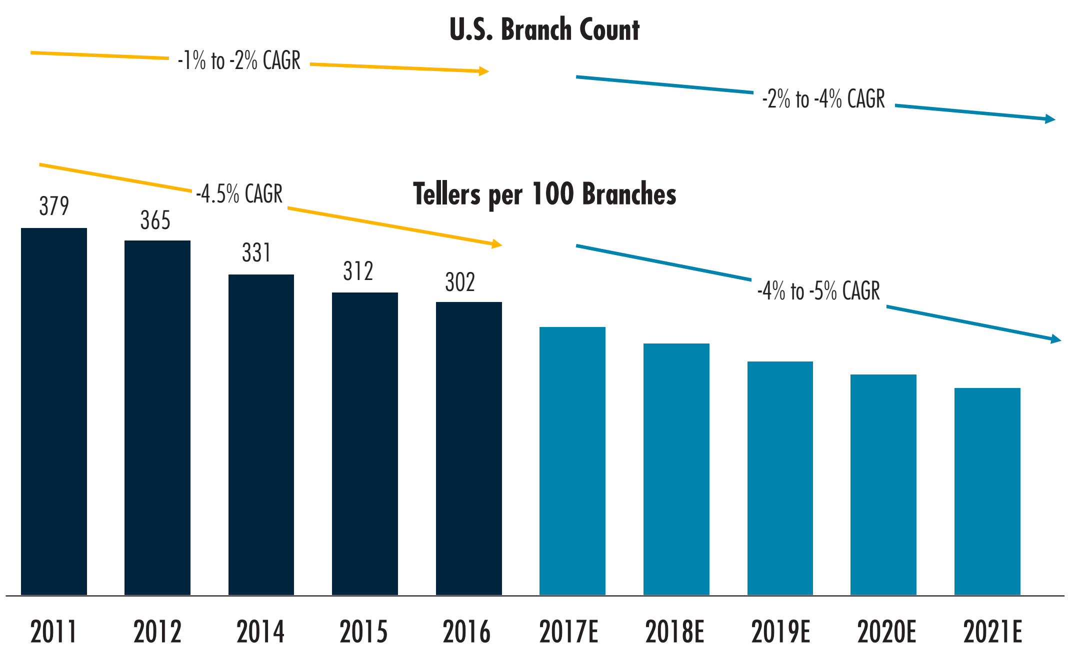
First, the substitution effect is real with image deposits leading the way. With new technology such as ATM digital imaging, mobile phone cameras, and OCR software, banks can now digitally receive checks for deposit, directly displacing teller activity and branch visits. Customers are rewarded with new convenience and enjoy expanded service outside of branch hours, not to mention better availability. With such a powerful precedent in place (substitution with an appealing customer benefit), the stage is set for accelerated digitization.

Second, the financial urgency is real. Branch reductions can be a primary source of cost savings, needed not only to improve profitability, but also to fund critical transitions to digital channels and offerings. Accelerating channel substitution paves the way, but must be managed correctly. Yanking the rug out can provoke customer defection rather than growth, with a direct impact on core deposit formation.

Third, the competitive urgency is real. While most banks now offer remote deposit capture via mobile and ATMs, the largest banks have led the way and seen

FIGURE 1: Mandate for Further Transaction Automation

Staff efficiency and branch consolidation will need to accelerate, and consumer digital migration will be essential to progress.

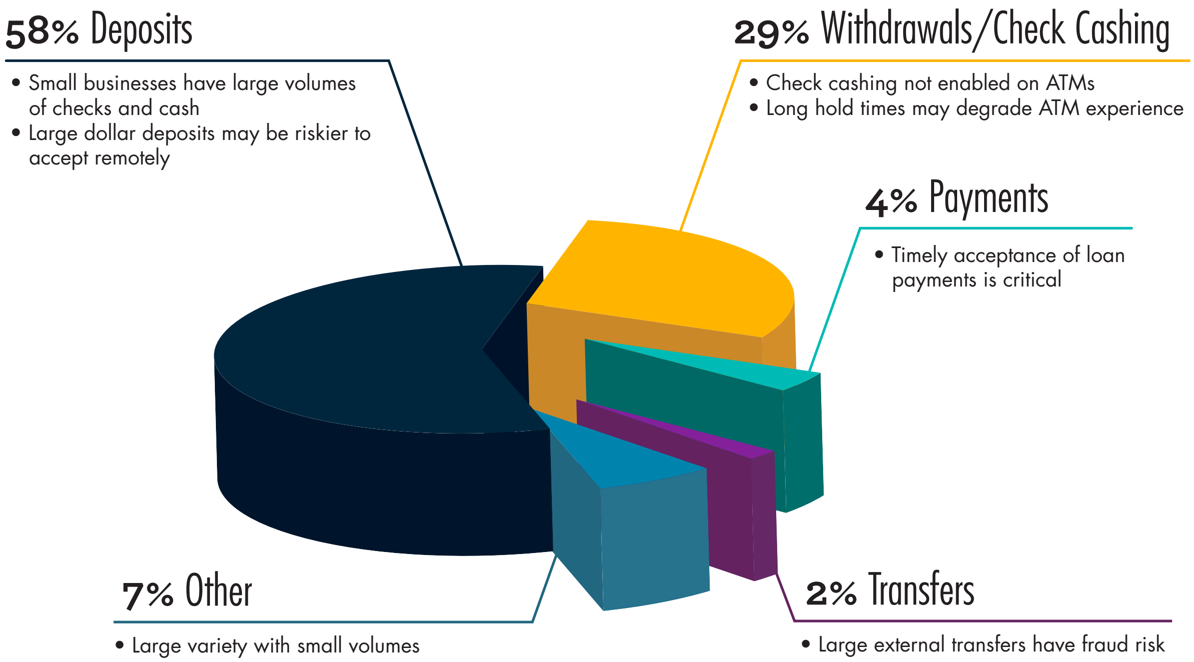


* Teller FTE as of second quarter of the year

Source: Novantas's SalesScape

FIGURE 2: Breaking the Barriers to Further Migration

Following early substantial progress with deposit migration, remaining branch transactions will be more difficult to migrate.



Other category includes Account Maintenance, Admin Corrections, Card Maintenance, Checking Inquiry, Close Account, Fee reversals, New Accounts, Stop Payments, Portal Inquiry

Source: Novantas's SalesScape

both better customer acquisition rates and lower branch usage. In contrast, other banks have taken a "build it and they will come" posture, with weak change management support. The result: weaker customer channel shift and lowered returns on automation technology investment. Meanwhile, the proactive players race ahead, realizing more digital migration benefits that permit further investment in additional initiatives.

Finally, migration efforts are one key element of a broader repositioning of the bank for an increasingly digital future. These investments are more than just tactical moves to capture near term efficiencies, enhance customer experiences and maintain customer loyalties. Migration programs also build long term digital capabilities and cultural changes that are core to reinventing the everyday banking experience.

STEPS IN MANAGING THE MIGRATION

To reach this optimal zone in digital migration and channel substitution, banks will need a holistic migration program that addresses critical questions and capabilities in the four major areas of measurement, segmentation, prioritization and execution (Figure 3: Keys to a Holistic Digital Migration Program).

The bank must develop sophisticated measurements of migration rates across channels over time for all transactions, service, and sales. Many activities were traditionally measured separately within different channel silos, depriving management of a full customer-centric view across all channel touchpoints.

In order to set effective migration targets, it is critical to see how customer behavior is changing and moving from one channel to another by transaction type. For example, a year-over-year view may indicate that deposits are still migrating to mobile, but ATM deposits are stalled. Some of the largest and most advanced institutions in the field of digital migration now have dedicated analytic teams to measure transaction activity across channels. We believe many others must and will follow.

The bank needs a deep understanding of different customer segments, their transaction patterns, and their likely migration rates. A particular focus is needed on behavioral drivers: where is channel migration stalled; what is preventing further switching; and what will motivate significant change.

For any transaction type, a small percentage of customers will generate the majority of transactions. Even among these customers, some will be using digital channels sparingly; others have never used them at all. Some will need face-to-face technology education; others may respond to promotion and/or incentives. Small business customers will need a separate and distinct plan, given their importance and different needs. So the actions a bank must take will differ by segment.

To prioritize properly, the bank needs a comparative analysis of potential rates of return on various automa-

FIGURE 3: Keys to a Holistic Digital Migration Program

For a solid digital migration program, banks need to develop capabilities in four key areas: measurement, segmentation, prioritization, and execution.

MEASUREMENT
- Migration rates by channels for all transactions, service and sales
- Customer-level movements across channel by transaction type
- Dedicated analytics teams to measure activity across channels

SEGMENTATION
- Deep understanding of transaction behavior by segment
- Barriers to further segment migration; what will it take to overcome
- Segment migration scenario.

PRIORITIZATION
- Business cases and ROIs for potential digital investments
- Key assumptions, incentives
- Best path of projects over time

EXECUTION
- Cross-functional migration project roadmap, with project office
- Branch-level migration targets by transaction type
- Training, incentives, metrics, customer feedback loops

Source: Novantas

tion investments. Often priorities are set without an apples-to-apples business case analysis. Specifically, all migratable channel activities must be analyzed and financially quantified. Current transaction volumes and associated costs must be determined. For example, if customers are checking current balances by calling the contact center or visiting their branch banker, the total cost of this service can be computed.

Then a realistic projection of migration rates to automated channels is needed. In many cases, the bank has already provided digital options for customer activities, but activation and usage rates still lag. Here, incremental outlays may be required — e.g., marketing, communications, employee incentives — to accelerate customer transitions.

Also, a bit of creativity helps in evaluating the best way to support a particular digital migration objective. For example, instead of encouraging customers to use mobile banking to check their account balances, perhaps real-time alerts and balance updates could be provided following transactions, negating the need to "look-up" information.

A better sense of digital priorities will emerge as this migration investment analysis is completed across the full spectrum of transactions, service, and sales.

Finally, the bank needs a cross-functional migration execution program. A "migration project office" is needed to influence and track substitution behaviors and resulting staffing levels. Great execution begins with a realistic plan. Channel migration is challenging because it requires teamwork and coordination across areas such as retail, digital, marketing, and real estate.

For example, many banks are retooling branch formats to reduce space for teller lines while providing more ATMs and digital stations for self-service or assisted-service. These reformats are challenging to execute without disrupting the customer experience, and the level of synchronization required is similar to the complexities of a new store opening or a product launch. Yet even more of this type of activity is necessary if the full benefits of migration are to be realized.

An additional benefit of digital migration is that customers begin to relax their general sense of branch dependence, becoming less likely to leave the bank when it reformats, combines or closes traditional branches. Novantas research shows that the closure attrition impact is much lower for multi-channel or digitally-centric customers than for branch traditionalists. Increasing digital adoption across transaction, service, and sales dimensions will support not only the reduction of FTE staffing requirements, but will also allow for the large, "chunky" cost take-outs provided by branch closures.

DIGITAL MIGRATION PRIORITIES

The levels of branch consolidation and staff operating efficiency needed for future digital-centric competition simply cannot be achieved without extensive customer channel substitution. Once executives understand this, they will place digital migration high on their list of corporate priorities.

Most of the early action in digital migration has centered on deposit activities, but deposit migration is just the beginning of a long journey to digitize all aspects of the banking experience. New technologies are unlocking a large number of opportunities across transactions, service, and sales.

In fact, the "shopping" component of bank sales has already substantially gone online, and as sales fulfillment improves, even more change is in store. In combination, this expanded array of revenue and efficiency initiatives will generate self-funding for additional digital investments and simultaneously transform the bank into a true omni-channel organization.

The catch is proactive management of customer migration. Coordinated efforts across functions (e.g., marketing, finance, and staffing) are needed to set, measure, and achieve migration targets. To accelerate the journey, many banks are in need of a holistic planning exercise in 2017 that begins to address the specifics of this challenge.

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