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Banking for Success: Using Analytics to Grow Wallet Share

WHITE PAPER

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SITUATION OVERVIEW

There has been a dramatic downward shift in consumer bank profits, and institutions now are creatively building a foundation for future profits. Part of the approach is careful analysis of current clients and prospects to determine how regulatory and other market changes have altered customer profitability. As a follow-up, banks are using that information to promote appropriate products to consumers and to ensure that appropriate service and pricing levels are employed. By focusing on the value of relationships, banks can both reward their best customers and prompt unprofitable segments to adjust their behavior — either to acquire more profitable products or to move their business to another financial institution. This new world of banking and customer profitability has spawned a new set of approaches and technology deployments that focus on consumer analytics — which involves the analysis of customer data to improve marketing, sales, service, and interactions.

Marketing

Targeted consumer marketing is a mature, metrics-driven business, but it is a business in transition. To grow their retail businesses, banks must increase their cross-sell effectiveness, as this is one of the leading indicators of profitability and low customer churn rates. However, to succeed, banks need to go beyond generic offers of products and services to all of their customers and begin targeting more specific customer segments. This improved segmentation should be based on behaviors, not just demographics, and allow the bank to develop products and pricing offers that appeal to the target segments. This will allow the bank to focus offers on those customers that are most likely to respond and increase cross-sell offer acceptance.

The tools to accomplish this goal, however, are in transition. Banks have traditionally depended on the customer information they had within their walls, enhanced with outside credit data and other sources, to improve marketing to their customer base and new prospects. This data was then combined with rules-based analysis tools, which were used to compare prospects to known criteria and then match these prospects to available bank products. Today, however, state of the art is quite different. These models can analyze multiple scenarios against individual prospects and then match the offer most likely to be accepted to each customer. With advanced analytical software and data management tools, scenarios that used to take days to calculate can now be run in seconds and therefore increase the probability of making the right offer, to the right customer, at the right time. By incorporating actual results of marketing programs and offer acceptances back into these models, the predictions become more accurate and effective over time.

Relationship Banking

Banks must embrace relationship banking to grow, and to do that they must find ways to cross product silos within their institutions. Relationship-based pricing is a great idea, but it requires a strong technology infrastructure to make it happen. Institutions not only require access to data (within the institution and from external sources) but must have an ability to understand important elements within the data and how to appropriately act upon findings that result from data analysis. By analyzing customer data, banks can gain the following:

- A complete view of the customer, including the products the customer uses, typical behavior, and interactions the customer has had with the financial institution.

- Knowledge of how customers behave and what rewards and/or services they value (fees, interest, maintaining balances, loyalty programs, etc.)

- The products customers are buying from other providers and why

- The outcome of previous interactions with the bank — across all channels

However, banks must also ensure that they are working within the constraints of consumer protection rules. Unlike other organizations, banks must ensure they are using fair and consistent lending practices, sharing information appropriately and securing personally identifiable data. Banks must be cognizant of these constraints and ensure that they are using analysis and scoring techniques that can be audited and that are acceptable to regulators.

In addition to technological barriers, there are also organizational issues that must be considered. Institutions that are crossing internal silos effectively are taking a pragmatic approach — for instance, working across card and deposit accounts first, then bringing in mortgage, consumer lending, and/or wealth management groups once the value of collaboration can be proven. Fortunately, the goals for all of these groups are similar and tied to an institution's overall profitability — banks must encourage clients to purchase more financial products and reward those clients with better pricing and/or more services. And it is only by capturing and analyzing the full set of products clients are using, along with transaction history, that banks can get to relationship banking.

Profiting from Customer Interactions

Analytics and data management have long been deployed to build more effective marketing programs, and the next big opportunity is to use these same tools to improve branch, call center, and/or online channel effectiveness. The branch is the bank's most expensive channel and is theoretically designed to maximize increasingly infrequent in-person customer interactions. However, for almost all banks, the theory has not been effectively put into practice. Customers are using branches less often, and banks need to make the most of those in-person interactions by arming their staff with information so they can confidently suggest financial products and solve customer problems.

What we typically see in branches or call centers are staff who are more focused on transaction processing or servicing than extending relationships with their customers. Bank tellers and call center employees are typically not equipped with the insight they need to offer the products that match customer needs. Nor do they have a view into products that have already been offered to customers and their responses. For banks to improve the sales culture in their branch networks, branch staff must learn how to become financial advisors, and they must be supported in their efforts to provide good advice.

Part of that transition from transaction processing to financial advice requires a commitment to multichannel banking. Institutions that can provide customers with self-service options as part of their online banking solution will reduce the number of branch visits for basic transactions. Alternate channels must also be enhanced to provide relevant marketing messages and actionable capabilities so that customers can both shop prices and close new business online.

Although many banks still believe that more branch traffic is good for business, the opposite is really more desirable. Moving simple transactions out of the branch frees up staff to focus on sales and service and allows staff the time they need to work with customers and respond to inquiries appropriately. Institutions that can focus their branches to serve complex customer service issues or respond effectively to product and sales inquiries are on their way to transitioning from transaction processors to financial advisors.

Defining the Benefits of Customer Analytics

IDC leveraged its extensive interviews with analytics banking end users and created a scenario to illustrate the potential benefits for a completely deployed analytics solution. This combined solution approach enabled IDC to quantify the benefits of this technology in conjunction with the best practices for implementing a customer analytics solution.

The solution delivers benefits in three areas:

- **Improve consumer marketing.** Institutions that make investments in analytics improve the efficiency and accuracy of their marketing efforts. With improved analysis, they can make better offers to a better qualified group of prospects — they send out fewer offers (lowering costs) but get more responses (increasing revenue). Results institutions can expect include:

    - **Reduce marketing costs.** Analytics can be used to improve the predictability of acceptable offers. Those prospects that are unlikely to respond can be eliminated from campaigns, and focusing on highly likely prospects can reduce the cost of mailings and promotions by as much as 80%.

    - **Increase revenue generation.** Certainly, institutions can improve response rates and boost revenue by offering above-market deposit rates or very attractive loan terms. They can achieve very high response rates, but revenue generation is not maximized. Further, institutions engaging in these practices attract a volatile customer base that will jump ship when they get a better offer from another bank. With analytics, institutions can test multiple scenarios and choose product offers that are compelling but also strike the right hurdle rates for the institution. So part of the story is increased response rates, by as much as 350%, but just as compelling is the ability to meet profitability targets with the right product mix.

    - **Increase efficiency of data analysis.** With a managed data solution, marketing staff can reduce the time spent locating data sources, performing analyses, and creating reports.

- **Increase wallet share.** Institutions continue to bring in new customers, but there is even more opportunity in selling additional products to existing customers. Fortunately, institutions already have a huge amount of data on existing customers that can be leveraged to improve both marketing effectiveness and customer service. Institutions can:

    - **Increase products per customer.** Financial institutions have mature approaches to customer segmentation and product offerings, but most have not developed relationship pricing approaches to reward their best customers and improve wallet share with their less-affiliated clients. Institutions with a successful approach can expect to increase the number of products per customer and average revenue by 4%.

    - **Reduce customer churn.** With a relationship focus and next-best-product strategies that are individualized for each customer, institutions can reward their best customers and increase the likelihood that they will remain loyal. If banks so choose, they can also more accurately identify those clients that drain bank profits and deploy strategies to either entice them with new products or steer them toward alternative financial service providers. This could reduce customer churn by 13% by providing custom services targeted to specific needs. The benefits include reducing both the partial loss of revenue and the administrative and marketing costs to replace each customer lost.

- **Reduce default rates.** Customer analytics enable banks to be more selective in their loan offers and decisioning. With less predictability from standard measures such as credit reports, institutions must develop internal approaches to determining credit worthiness. Those that can harness the power of their own data and analytics will be in a better position to grant loans to attractive candidates and will know which candidates are poor risks. For example:

    - Institutions that have chosen to respond to the changing market by simply increasing credit rating thresholds are faced with a diminished pool of candidates, and they are less able to deploy their capital balances. By changing their decisioning and using other predictive measures, they can put their cash reserves to work and earn higher returns for the institution.

    - Once loans have moved into collection, institutions are deploying analytics to determine appropriate collection processes for each borrower. In this way, banks can improve collection rates and handle customers in a manner that will ideally lead to their becoming customers in good standing again.

Industry Scenario

To put the benefits of an analytics solution in the context of how its deployment would impact a retail bank, IDC built the scenario shown in Table 1.

As an example of how investments in customer analytics can benefit, a typical scenario has been developed. Using the bank characteristics shown in Figure 1, IDC Financial Insights used information provided by actual banks to develop a financial benefits model associated with customer analytics. In Table 2, we focus on one element of customer analytics — more effective marketing. As shown in Table 2, this institution was able to increase response and conversion rates by presenting customers with more appropriate offers. The institution was also able to increase effectiveness by doubling the number of campaigns executed each year because of increased processing throughput. Some institutions choose to use enhanced throughput to refine offers by creating many iterations before fielding the best options. Others choose to use the increased capacity to simply conduct more campaigns.

TABLE 1

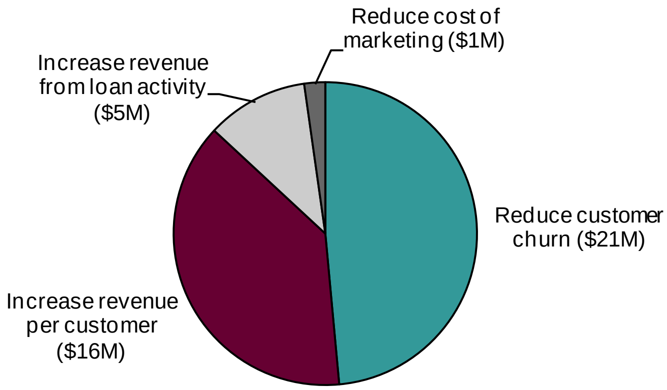
Retail Bank Scenario

Category	Detail
Employees	5,000
Customers	10 million
Revenue ($M)	2,750
Benefits from customer analytics ($M)	43

Source: IDC Financial Insights, 2012

FIGURE 1

Potential Annual Benefits from Customer Analytics



Total benefits = $43M

Source: IDC Financial Insights, 2012

TABLE 2

Customer Analytics: Measuring Marketing Effectiveness

Marketing Effectiveness: Accurate Marketing Targeted to High-Value Customers	Before	After	Change
Target market (number of prospects)	5,000,000	1,000,000	4,000,000
Response rate (%)	1	5	4
Convert to sale (%)	.06	.09	.03
Incremental sales (new customers)	3,000	4,050	1,050
Annual marketing costs ($)	300,000	60,000	240,000
Average cost per new customer ($)	100	15	85
Number of campaigns per year	12	20	8
Total savings per year ($)			960,000

Source: IDC Financial Insights, 2012

First Tennessee Bank

By transforming its approach to data and analysis, First Tennessee Bank has dramatically increased its marketing effectiveness. This is a bank that understands that measuring effective marketing must include realized compared with potential customer profitability as opposed to measuring just the number of new products sold. As every marketer knows, if you simply make an offer attractive enough, sales will follow. Many banks pursue this strategy to increase deposit rates — offering high interest accounts to bring in new business — but lose those customers as soon as a competitor has a better offer. Customers brought in by overly attractive offers are not only less loyal but also less profitable. Using analytics effectively allows banks to manipulate offer attributes, in a very granular way, to achieve higher profitability from a growing customer base. First Tennessee uses models they have developed internally to create profitability tiers with varying product attributes. The bank has also developed customer scoring models, based on very granular data points, to determine each customer's likelihood to purchase potential offers. With these product and customer models, the bank can create profitability scenarios and use these to determine which product offers will generate the most value for the bank. The bank then uses this information to prioritize marketing programs and allocate resources effectively.

As a result of this approach, First Tennessee has produced quantifiable results. It has cut its mailing and printing marketing costs by 20% and 17%, respectively, by allocating resources more effectively. And at the same time, it has increased effectiveness — generating a 3.1% increase in response rates by putting better offers in front of its prospects without sacrificing profit targets.

ESSENTIAL GUIDANCE

Financial institutions investing in customer analytics will find that they have the ability to build profits back in to their consumer banking businesses. With limits placed on fees they can generate from interchange and overdraft fees, banks are reevaluating their customer and product mix. Those that use state-of-the-art tools will reap benefits in improved customer insight. With marketing programs enhanced by analytics, banks can see improvements similar to those reported by First Tennessee. They can also focus on improving customer relationship management — rewarding their best customers with attractive pricing and serving customers better through appropriate channels.

To develop thriving consumer banking businesses, institutions need better tools to evaluate their current customer and product sets and to attract their next set of profitable customers. Institutions also must keep those customers loyal to the bank and ensure that they are capturing at least their fair share of customer wallets.

Improving customer insight serves many masters — it will improve marketing results, improve customer experience across channels, build a path to relationship banking, and improve sales effectiveness and customer profitability.