**EMERGING ISSUES IN RETAIL BANKING**

1. **Knowing Customer (Commercial/Business Perspective)** 
   * ‘Know your Customer’(KYC) has also become an important Regulatory Requirement
   * In order that the product lines are targeted at the right customers-present and prospective-it is imperative that an integrated view of customers is available to the banks
   * The benefits flowing out of cross-selling and up-selling require vital inputs
   * What needs to be done is setting up of a robust data warehouse where from meaningful data on customers, their preferences, there spending patterns, etc. can be mined
   * Cleansing of existing data is the first step in this direction
2. **Technology Issues** 
   * Retail banking calls for huge investments in technology
   * Whether it is setting up of a Customer Relationship Management System or Establishing Loan Process Automation or providing anytime, anywhere convenience to the vast number of customers or establishing channel/product/customer profitability, technology plays a pivotal role
   * The Issues involved include adoption of the right technology at the right time and at the same time ensuring volumes and margins to sustain the investments
   * It is pertinent to remember that a large international bank, known for its deployment of technology, took quite a while to make profits in credit cards
   * However, without adequate technology support it would be almost impossible to administer the growing retail portfolio without allowing its health to deteriorate
   * Further, the key to reduction in transaction costs simultaneously with increase in ability to handle huge volumes of business lies only in technology adoption
   * Lack of connectivity, stand alone models, concept of branch customer as against bank customer, lack of convergence amongst available channels, absence of customer profiling, lack of proper decision support systems, etc., are a few deficiencies that are being encountered
   * The initiatives in this regard should include creating flexible computing architecture amenable to changes and having scalability, a futuristic approach, networking across channels, development of a strong Customer Information Systems (CIS) and adopting Customer Relationship Management (CRM) models for getting a 360 degree view of the customer
3. **Organizational Alignment** 
   * It is of utmost importance that the culture and practices of an institution support its stated goals
   * Having decided to take a plunge into retail banking, banks need to have a well defined business strategy based on the competitive position of the bank and its potential
   * Creation of a proper organization structure and business/operating models which would facilitate easy work flow are the needs of the hour
   * The need for building the organizational capacity to achieve the desired results cannot be overstated
   * This would mean a strong commitment at all levels, intensive training of the rank and file, putting in place a proper incentive scheme, etc.

As a part of organizational alignment, there is also the need for setting up of an effective Corporate Marketing Division. Most of the banks have only publicity departments and not marketing setup

A full fledged marketing department or division would help in evolving a brand strategy, address the issue of alienation from the upwardly mobile, high net worth customer group and improve the recall value of the institution and its products by arresting the trend of getting receded from public memory

The much needed tie-ups with manufacturers/distributors/builders will also be facilitated smoothly

It is time to break the myth that banks are not customer friendly. The attention is to be diverted to vast databases of customers lying with them still unexploited for marketing

1. **Product Innovation** 
   * Product innovation continues to be yet another major challenge
   * What is of crucial importance is the need to understand the difference between novelty and innovation? Peter Drucker in his path breaking book: “Management Challenges for the 21st Century” has in fact sounded a word of caution: “innovation that is not in tune with the strategic realities will not work; confusing novelty with innovation should be avoided, test of innovation is that it creates value; novelty creates only amusement”
   * Banks need to innovate products suiting the needs and requirements of different types of customers. Revisiting the features of the existing products to continue to keep them on demand should not also be lost sight of
2. **Pricing of Product** 
   * The next challenge is to have appropriate pricing policies in place
   * The industry today is witnessing a price war, with each bank wanting to have a larger slice of the cake, without much of a scientific study into the cost of funds involved, margins, etc.
   * Most of the banks that use rating models for determining the health of the retail portfolio do not use them for pricing the products. The much needed transparency in pricing is also missing, with many hidden charges and to camouflage the price
   * The situation cannot remain this way for long. This will be one issue that will be gaining importance in the near future
3. **Process Changes** 
   * Business Process Re-engineering is yet another key requirement for banks to handle the growing retail portfolio
   * Simplified processes and aligning them around delivery of customer service impinging on reducing customer touch-points are of essence
   * A realization has to be drawn that automating the inefficiencies will not help anyone and continuing the old processes with new technology would only make the organization more inefficient
   * Work flow and document management will be integral part of process changes
   * The documentation issues have to remain simple both in terms of documents to be submitted by the customer at the time of loan application and those to be executed upon sanction
4. **Human Resources** 
   * While technology and product innovation are vital, the soft issues concerning the human capital of the banks are more vital
   * The corporate initiatives need to focus on bringing around a frontline revolution. Though the changes envisaged are seen at the frontline, the initiatives have to really come from the ‘back end’
   * The top management of banks must be seen as practicing what it preaches
   * The initiatives should aim at improved delivery time and methods of approach.
   * There is an imperative need to create a perception that the banks are market-oriented
   * This would mean a lot of proactive steps at various levels, devising appropriate tools for performance measurement bringing about a transformation ' ‘can’t do' to 'can do’ mind-set change from restrictive practices to flexible work place:
     + By having universal tellers,
     + bringing in managerial controlling work place,
     + provision of intensive training on products and processes,
     + emphasizing coaching, etiquettes, good manners and best behavioral models, formulating objective appraisals,
     + putting in place good and acceptable reward and punishment system,
     + facilitating the placement of young /youthful staff in front-line,
     + defining a new role for front-line staff by projecting them as sellers of products rather than clerks at work,
     + changing the image of the banks from a transaction provider to a solution provider
5. **Rural Orientation** 
   * As of now, action that is taking place on the retail front is by and large confined to major cities

* + There is still a vast market available in rural Pakistan, which remains to be tapped
  + MNCs, as manufacturers and distributors, have already taken the lead in showing the way by coming out with exquisite products, packaging and promotions, keeping the rural customer in mind
  + Some FMCGs made available through an efficient network add testimony to the determination of the MNCs to penetrate the rural market. In this scenario, banks cannot lack behind
  + In particular banks having a strong rural presence, need to address the needs of rural customers in a big way. These and only these will propel retail growth that is envisaged as a key strategy for portfolio expansion by most of the banks

1. **Financial Exclusion** 
   * The scope of enhancement of Banking Business in Pakistan is considerable as the level of *Financial* *Exclusion* is exceptionally high despite the growth in Banking
   * Penetration ratio of financial services is low judged by any measures as less than 20% of the population has access to financial services and number of borrowers are under 5 million (3% of population)
   * More graphically, **there are only 171 deposit accounts per 1,000 people and 30 loan accounts** **per 1,000 people**
   * Likewise, only 30% of adults have bank accounts
   * Credit/GDP ratio at 27% is low judged by country and sector financing requirements or judged by levels prevailing in Emerging Markets
   * Consumer financing penetration ratio is 3.9%

**Distinguishing Features of a typical Consumer Banking (CB) Segment of a Bank in Pakistan**

* CB is a Scale Sensitive, Mass Market, & Volume business
* Standardized Processes & Procedures
* Substantial upfront outlay for Designing, Developing, Marketing, Distributing, & Delivering various products
* Adherence to SBP Risk Management Guidelines
* Separate organizational setup for post-sale issues like Collection, Recovery, Litigation etc.
* Multiple Delivery Channels/Call Centers/Recorded Phone Lines
* Enhancing customer experience through effective/efficient management of “Customer Touch Points”
* Dedicated Sales & Service teams(Usually contractual)
* Hiring of external agencies for verifying & documenting details of customer profile and income source/estimation
* Professional Property Valuators
* Customer Segmentations under Life-Cycle parameters
* Adherence to Transfer Pricing regime for determining true profitability of products/services
* Innovative personal saving /investment products through Alliances with Insurance Companies & other financial service providers
* Service Level Agreements (SLA) with bank own support functions like Operations, IT, HR etc
* Brand Affiliation/Channel Partnering

**New Segmentation Approaches to Drive Product Innovation**

**Innovation in Segmentation Strategy**

Although banks have practiced customer segmentation for the past decade or so, there is room for further refinement of their strategies. Having moved from a product-centric to a customer-centric approach, banks continue to employ broad brushstrokes to segment their customer base. In doing so, the risk attributing common characteristics to a large number of customers who may have been grouped together on the basis of a single parameter, such as relationship value. More importantly, their product and service offerings are likely to be tailored to the perceived needs of these segments. At the same time, banking customers continue to demand more. They are no longer content to be viewed as faceless constituents of a large group; rather, they expect their banks to recognize their individual needs and offer custom-made solutions to help them achieve their financial goals. Against this backdrop, banks must become more innovative in the way they view their customers as well as the manner in which they serve them.

**Beyond Relationship-Value Segmentation**

For a start, banks can look at refining customer segmentation by taking a multi -dimensional approach that goes beyond relationship-value. While segmentation on the basis of relationship value is important in order to recognize and reward customer loyalty, it falls short of enabling banks to identify and attract new business opportunities. It is also possible that customers with vastly different relationship-values may be connected in other ways, and therefore, could be part of the same segment from an entirely different standpoint. Hence, banks need an in-depth, well-rounded perspective of their customers before they can categorize them. This perspective must consider various factors besides relationship value including but not limited to, demography, geography, ethnicity, gender and profession. As a matter of fact, banks are well placed to do so, since most, if not all of this information would already be available within their database. Analysis of comprehensive customer data can reveal homogeneous patterns that can be used to create new and more meaningful customer segments which can be targeted for tailor-made products and services.

**New Approaches to Segmentation**

Customer segmentation on the basis of homogeneity of behavior, aspiration, value, culture or habit can bring to light specific opportunities which may not be visible when only relationship value is taken into consideration. It is intuitive that those who share a common geography, language, profession or social status will also have, to a certain extent, similar values or behavior. Therein lies vast, untapped opportunity – if banks can offer products and services that support such homogeneity, they are likely to reap big benefits by way of new business and cross-sales. This view is best illustrated with some examples:

* A couple of prominent U.S. banks have gone after the 37 million-strong Hispanic population, considered an unprofitable customer segment by most of their peers. This group has very specific requirements – the facility to deposit pay-checks, make money transfers and maintain a zero balance in their account being the most important. The banks have accordingly introduced innovative products tailored to these needs. One bank offers more options to move money: as cash to cash or as cash to accounts or cards, being some of them. They also allow their customers to cash pay-checks. The other bank has pioneered a special zero minimum balance account just for Hispanic clients
* Geographic segmentation is another important possibility. A physical location can be a great determinant of customer needs – for instance, while all agricultural regions have large demand for farm loans or short-term trade financing, their demand patterns differ based on the crop and harvesting cycle. Another example is that of customers on the West and East Coast of the U.S., who hold different financial aspirations which cannot be met with the same suite of products. Although regional and rural banks cater to geographic diversity to a certain extent, national banks can follow suit by creating location-based sub-segments and targeting them. With different offerings Segmentation by social strata is gaining currency riding on the concept of financial inclusion. The world over, banks are innovating their product and channel strategy to reach out to the unranked population. Going forward, they must attempt to discover subtle patterns within these segments, so that they can target smaller sections with customized offers
* Different generations display distinct behavioral patterns. Aging baby boomers may seek personal guidance while planning their retirement savings; not so the tech-savvy and self-reliant Generation X. The “digital native” Gen Y is technologically ahead of them all, and is at ease transacting over the Internet, mobile phone or even social networking platforms
* Segmentation-driven innovation need not be confined to products alone. Several Canadian banks have set up multi-lingual branches, where employees speak up to eight languages, to cater to the vast expatriate community in that country. ATMs in rural India offer screens in vernacular languages to encourage usage among the resident population
* Banks can also benefit by segmenting their customer base along unconventional dimensions. An Australian bank offered a utility bill payment service in the form of a specialized loan to those customers who had difficulty keeping up with their monthly payments. By doing so, they earned interest from their customers and commission from the service providers. New methods of segmentation have also been considered within niche areas such as wealth management, with sub-segments being formed on the basis of source of wealth, customer sophistication, life stage and geography
* Another approach advocates the formation of customer groups depending on their banking behavior – which is either investment or borrowing/transaction oriented. Typically investors

comprise older, more affluent clients who maintain high balances and are primarily concerned with growing their wealth for the future. Since this group is not focused on deposit products, it is not very sensitive to interest rates

* On the other hand, lower-balance transactions are young and just starting to accumulate wealth through employer plans, IRAs or similar avenues. Mostly, their needs are immediate – and hence, they lay greater emphasis on checking, saving and loan products and the interest rates associated with each
* Not surprisingly, their channel preferences also differ. High-balance customers want experienced branch staffers to whom they can turn in case of need. Their low-balance counterparts are happy using self-assisted channels such as PC/Internet banking, ATMs and call centers
* Clearly, banks need very different strategies to tackle each of these groups. At the same time, they must recognize the interplay of multiple factors within each segment – for instance, some members of the Hispanic segment may have similar social, linguistic and economic characteristics. Another example of this is evident in the case of the high-balance investors discussed earlier, who, apart from having common financial goals, may also be at a similar life-stage. Thus, going forward, banks’ segmentation strategy must create finer “sub- segments” which are homogenous along different dimensions. This will lead them from customer-centricity to the more desirable state of customer-specificity or “segment of one”. For instance, of the three broad customer segments, namely corporate, small business and retail, the latter can be grouped by generation, which in turn may be segmented according to geography, income, behavior and so on. The corporate and small business client base can be similarly broken down

**Innovating to Create Relevant Products and Services**

That being said, a sophisticated segmentation strategy will achieve little unless it is backed up by innovative products and services relevant to the needs of different groups. Hence, banks need to map their “offerings” defined by a combination of product, price, channel, timing and human resources to various customer segments. For instance, they can bundle a set of investment products for their Gen X customers and train a team of relationship managers to deliver them. Another example is the creation of small savings products to cater to the new savings consciousness emerging in the aftermath of the global crisis. Banks must also give due weightage to pricing to ensure that small- ticket vanilla products are not perceived as being expensive by the target segments. Timing is equally important – Gen Y customers have simpler, frequent needs and expect instant fulfillment, whereas mature clients are likely to have significant requirements at different life-stages, such as marriage, parenthood or retirement. A well-rounded segmentation approach must take all this and more into consideration.

**Aligning the Organization with a Robust Segmentation Strategy**

While all of this is good wisdom, it is only part of the story. The goal of true segmentation is not merely to offer innovative products and services, but to ensure that the customer experience is raised to a different level. Hence, the entire banking organization, including its policies, processes and people must be aligned with the segmentation strategy. KYC norms are a good example of how policies can be “turned on their heads” to support segmentation – rather than following these norms purely as a compliance practice, banks can use the information to strengthen their understanding of various customer segments.

It goes without saying that banks will need resources as well as infrastructure to effect these changes. A sound technology platform is a necessary enabler at every stage – from segmentation to product innovation to customer experience delivery. To start with, banks need a 360 degree unified view of their customers across the organization – only integrated core systems have the capability to consistently deliver this information, no matter how large the scale. Technology is required to analyze huge volumes of customer data, discover patterns within them and engender the progression of broad-based segmentation to a “segment of one”. Again, quick roll-out of new products and services is only possible with the support of modern core banking systems. The same systems enable banks to optimize their channels and processes, making them more efficient but not less personalized, all of which contribute to the delivery of good customer experience. For instance, technology can be used to trigger an investment recommendation whenever a customer's account receives sizeable inflows as well as alert the concerned relationship manager so that he may follow it up.

**Summary**

Banking customers' demands have kept pace with the rising complexity of their needs. They expect banks to address their individual requirements with relevant products and services. This implies that banking institutions must acquire a deeper understanding of their customers at a one-to -one level, and deploy that insight into product and service innovation. Customer segmentation is central to this objective.

Current segmentation practices are mostly uni-dimensional and based on a single parameter such as relationship value. Although the relevance of relationship value as a measure of customer loyalty is beyond doubt, it cannot be the sole criterion for segmentation. Going forward, banks must refine their segmentation strategy by taking into account a combination of demographic, social, economic, geographic and linguistic factors. Other innovative approaches to segmentation include grouping customers on the basis of financial behavior, customer sophistication or life-stage.

As broad customer segments are broken down into finer sub-groups, segmentation strategy shifts from customer-centricity towards customer- specificity. New business opportunities can be created by offering tailor-made products to each customer sub-segment. However, none of this is possible without the support of a strong technology backbone at every stage – whether it is the creation of new customer segments, roll-out of innovative offers or the alignment of processes and channels to provide a great banking experience across all segments.