

# Collaborative Customer Knowledge in Banking: A Guide to Strive and Thrive During Economic Turbulence and Beyond



**Kathleen Khirallah**

Managing Director  
Banking Practice  
February 2009

Compliments of



---

*TowerGroup Research is available on the Internet at [www.towergroup.com](http://www.towergroup.com)*

*© 2009 The Tower Group, Inc.*

*May not be reproduced by any means without express permission. All rights reserved.*

*TowerGroup is a wholly owned subsidiary of MasterCard Worldwide and operates as a separate business entity with complete editorial independence. MasterCard Worldwide is not responsible for and does not necessarily endorse any opinions, statements, or other content presented by TowerGroup.*

## Executive Summary

Bankers around the globe are prepared for a difficult 2009. Industry-wide challenges such as dealing with credit liquidity, capital adequacy, consumer confidence, regulatory reform, and deteriorating credit quality have ignited a seismic shift away from internally focused, business process-centric models toward those that focus more on the market and customers. This recalibration in business models was necessitated by the magnitude of the economic crisis and its anticipated duration.

Yet for many bankers, the current turmoil is providing opportunities for reassessment and regrouping for the future. The economic volatility that crippled financial markets in September and October 2008 will not last forever, and forward-thinking banks and financial institutions are already strategizing for the inevitable rebound in markets and institutional profitability. Although discretionary spending in banks (including IT spending) will be constrained, bankers have recognized that they can reflect on and evaluate their organizations, corporate cultures, and business models to effectively manage the financial crisis and position themselves for recovery.

Smart leading financial companies believe that the ability to see beyond the current economic turbulence and actively plan for the inevitable rebound is a key differentiator among competitors. As we see it, banks must continue playing both offense and defense as they execute their business plans. Offensively, they will look to the future and make bold decisions regarding their positioning in the marketplace; defensively, they will protect their existing profitable markets and customer share. That is, banks are embracing new customer-focused initiatives in an effort to retain their current profitable customers, protect their balance sheet through rigorous risk management, and pursue opportunities to maximize their operational efficiency as they simultaneously position themselves for a brighter future. This dual focus of short-term and longer-term strategic investment is at the crux of their goal to strive and thrive.

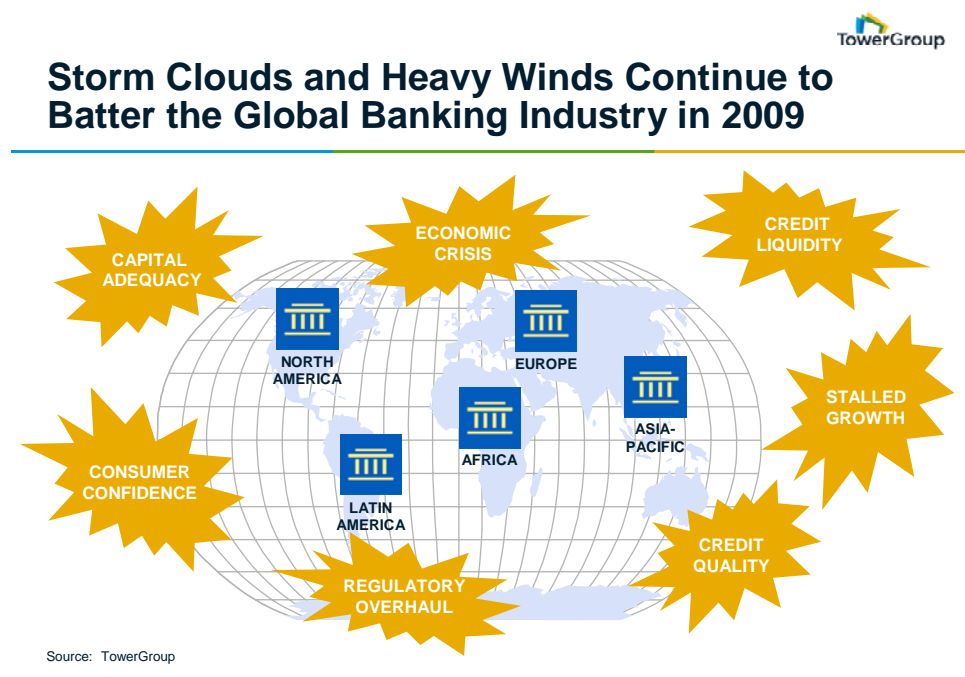
A key ingredient in this quest will be the collaborative use of customer knowledge across the enterprise. In past years, many banks have invested in optimizing their use of customer data, but only a few banks have made adequate progress in ensuring the availability of data and its collaborative use. Customer knowledge is a crucial corporate asset and of great value at the points of customer contact among all business units; banks are starting to focus on leveraging its use throughout the organization to survive through and succeed in the current market scenario.

TowerGroup believes that over the next few years, financial institutions have a business imperative to invest in new customer relationship management (CRM) capabilities that will allow them to leverage existing applications and investments to gain customer and business insight, scale, self-service capabilities, and process efficiency. Also, institutions will make the investment despite global economic uncertainty. Embracing this mandate will allow banks to differentiate themselves from their peers and position themselves for the inevitable economic recovery.

## Strive and Thrive Through the Economic Crisis

September and October 2008 will long be remembered as the time when the first, bitter fruits of the global economic crisis were harvested. Without question, institutional performance in the financial markets in 2008 was the worst in generations. Banks failed, insurance companies required propping up, hedge funds liquidated, stand-alone investment banks in the United States disappeared, and governments and regulators worldwide were forced to act decisively on an enormous scale. Market volatility was unprecedented. Given the velocity of the market downturn, it soon became clear that even decisive government action would not completely stem the tide; the ferocity of market sentiment was unstoppable. Exhibit 1 summarizes the ongoing challenges to the global economic system in 2009 and beyond.

### Exhibit 1



Fortunately for the banking industry, the current economic turbulence will come to an end. Economic uncertainty will clearly be the rule in 2009, but a rebound in the economy is inevitable. TowerGroup believes the primary challenge for banks will be to strategically prepare themselves for this change in economic conditions. Many organizations will spend the next few years in “survival mode,” reacting to daily events. Yet, the banks that are able to focus on the longer-term horizon and prepare for the rebound will be formidable competitors well positioned to increase their market share. Future financial success demands that banks move beyond “survive”

and focus on increasing market share and consequently on pleasing customers. To adequately position themselves for the future, banks need to increase their ability to be customer-centric, even as discretionary spending, and IT spending in particular, is constrained. Bankers must start investing in technology that enables them to serve customers appropriately and consistently while still driving scale, self-service capabilities, and process efficiency through automation.

Against a backdrop of economic uncertainty, bankers will play both offense and defense as they execute their business plans. On offense, they must look to the future and make bold decisions regarding their positioning in the marketplace, and on defense, they must protect their existing profits and markets. Three imperatives that banks need to get right starting now are:

- *Customer retention.* Retaining existing customers has become critically important as banks become ever more dependent on deposits as sources of funds. Expanding relationships with existing customers is equally vital.
- *Risk management.* Operating capital is scarcer now than at any time in recent memory. As a result, banks are significantly tightening requirements for credit underwriting at the same time governments are actively encouraging banks to increase their lending activity.
- *Operational efficiency.* Banks' efficiency ratios have increased greatly over the past 18 months, which is a worrying trend as the economic crisis continues.

Preparing for the future when the present is dire is not easy, but it is the hallmark of vision and solid strategy. Banks that embrace a strive-and-thrive philosophy will focus on improving the fundamentals of their business through efforts that will pay dividends when market conditions improve.

## **Collaborative Customer Knowledge**

The three strategic imperatives may not seem to be related on the surface, but they are all linked by a common solution: customer knowledge. Whether an institution is attempting to maintain its current market share, minimize its exposure to risk, or pursue additional efficiencies in its operations, customer knowledge is core to its efforts. Collaborative customer knowledge is a business strategy built on the premise that a rich understanding of customer information and sophisticated application of that information in business operations is integral to long-term growth. As an example, banks can most effectively collaborate on decisions about credit underwriting when business units and work groups share information. Financial institutions that wish to strive and thrive during the current crisis must embrace customer knowledge as their most valuable corporate asset.

### ***The Importance of Collaborative Customer Knowledge***

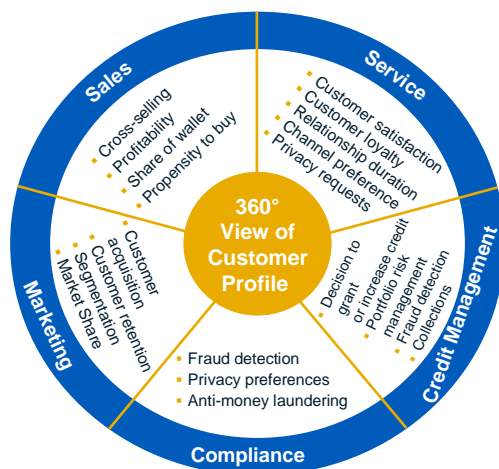
In recent years, customer satisfaction with banking relationships has been mediocre at best and customer loyalty has been equally dismal for most institutions. Because retaining customers and increasing share of wallet are pivotal to institutional profitability, institutions must open a rigorous audit of their customer knowledge capabilities and improve their competencies to give customers an optimal experience with them. The operative questions for most institutions are: "Is customer data centralized in a shared repository, and how well is that shared data leveraged within the bank and throughout all involved business lines?" TowerGroup believes that unless the data is readily available and reliable, major business metrics such as customer satisfaction, customer loyalty, and share of wallet will not improve. The reality of banking today is that multiple business functions rely on easily available and reliable customer data. Their ability to leverage it ultimately drives bank profitability. Exhibit 2 provides an overview of the ways customer knowledge, particularly in the form of a shared 360° view of customer relationships, can impact fundamental aspects of bank operations.

## Exhibit 2



### Centralized Data Repository Provides a 360° View of Customer for Multiple Purposes

---



Source: TowerGroup

---

As is clear from the exhibit, vital business needs such as sales, service, marketing, credit management, and compliance all benefit from a well-deployed strategy for managing customer knowledge. Key to an effective deployment of the strategy is a collaborative approach across an enterprise to deliver efficient results for both financial services organizations and customers.

#### ***Ability to Strive and Thrive with Collaborative Customer Knowledge***

For many banks, “thriving” during the current economic crisis seems like an elusive goal: highly desirable, but frustratingly out of reach. “Striving” to realize minimal levels of profitability may seem more realistic. The challenge, of course, is that banks must do both. They must strive for excellence in the current economic environment while positioning themselves to thrive after the eventual recovery. Banks cannot afford to view the next few years as a time for an “either/or” choice. Instead, they must embrace the challenge of “both/and” decisions. The ability to accept this dichotomy and successfully execute against it will be a fundamental differentiator.

To strive and thrive during the next five years, banks need to become experts at leveraging customer data across all aspects of their enterprise. Without question, the effort to aggregate the data in a centralized repository will give them a richer and more actionable view of customers and their relationships. Although an integrated 360° view of customer data offers

compelling benefits for sales, marketing, and service functions, the advantages to the institution go well beyond those realms, leading to stronger compliance, better risk management, and ultimately, more efficient operations.

## Customer Retention

Customer retention is an ever-present issue for banks, but it has increased in importance recently as banks compete aggressively for stable sources of low-cost funds and find themselves in the midst of a deposits battle.

In recent years, banks effectively moved assets off their balance sheets through the process of bundling loans by type (real estate, auto, credit card, etc.) and creating securities for sale to investors. They used the capital they received to fund new loans, and a virtuous circle of lending ensued. As real estate and other loans soured, investors became unwilling to purchase these types of asset backed securities (ABSs), and underwriters would not create and issue additional securities. Because banks were unable to move loans from their balance sheets via ABS issuance, they quickly became desperate for fresh sources of capital, increasing the importance of deposits, particularly those from existing customers.

As banks around the globe became enmeshed in a heated contest to retain customers and their deposits, interest rates paid on deposit accounts began inching higher. An escalation in interest rates has ensued, and banks have watched their profitability decrease as a result. Net interest margins have dropped to historic lows while banks' overall interest expense has increased markedly year over year. The clear lesson for banks is that simply paying higher rates of interest does not ensure adequate access to stable deposits. High rates will generate deposits, but the declining interest rate margin points to the concurrent drop in institutions' profitability.

To strive and thrive, banks in 2009 need to stem the outflows of deposits from existing customers while they implement plans to accelerate cross-selling of additional deposit products to that customer base. Because banks need to grow deposits, customer expansion will be as important as customer retention in the coming years. Retaining customers and driving an increase in share of wallet cannot occur without a more personalized approach to existing customers, however. Banks must parlay their knowledge of existing customers to understand customers' needs and make that information available across all business units so that they can offer quality services, relevant messaging, and ultimately, customer satisfaction.

## Risk Management

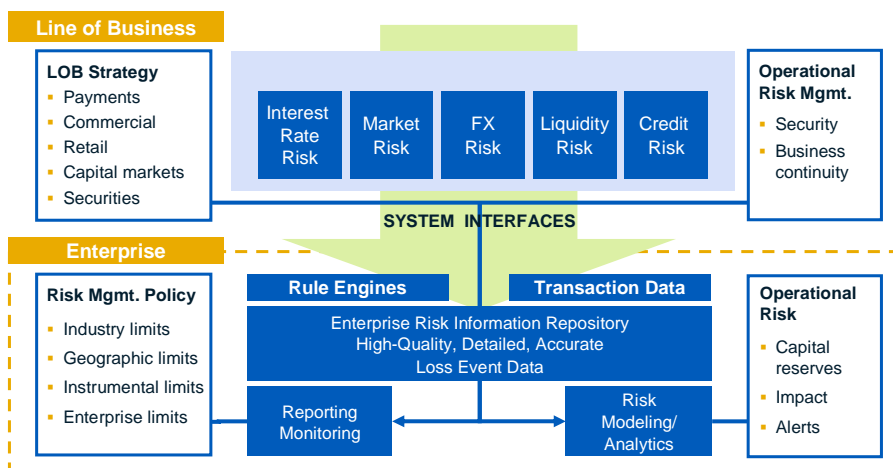
As too many banks now painfully understand, enterprise risk management will be a critical business competency in the near future. Not only will banks pursue it because it makes strong business sense, but regulators will insist that institutions become much more proficient in evaluating risk. The introduction of new banking regulations, particularly for credit risk, is a certainty starting in 2009. The role of the rating agencies in the current economic crisis is considerable, and banks will need to demonstrate internal expertise in managing risk to placate regulators.

As enterprises, banks need to address key indices of risk: customer limits, industry limits, geographic limits, instrument limits, and enterprise limits across the various lines of business (commercial, retail, payments, capital markets and securities). Simply put, enterprise risk management depends completely on the institution's ability to aggregate vital risk data and integrate the pieces into a mosaic that accurately reflects the institution's total risk exposure. Exhibit 3 provides an overview of the interconnections between line-of-business and enterprise assessments of risk.

### Exhibit 3



## Enterprise Risk Management Architecture



Source: TowerGroup

Critical to leveraging this enterprise view of risk is the element of data relevancy in subsequent analyses. The challenge before banks is not just to aggregate the risk information but also to understand its relevancy to business practices. Banks must go beyond simply aggregating data to introduce sophisticated analytics that allow for a contextual understanding of risk.

For bank customers (both consumer and corporate), the primary risk factor is credit. For banks to be truly effective at risk management at the enterprise level, they must evaluate customer credit risk at every stage of the loan, from the initial underwriting to collections and recovery. Thus, the collaborative use of customer knowledge is essential in improving the management of customer credit risk. Over the course of the lending relationship, a customer's financial profile can fluctuate radically. The sooner an institution can identify and react to degradations in customer financial profiles, such as payment delays or increases in overall debt ratio, the sooner it can take remedial actions. The challenge for banks is to become more adept at using the customer information available to monitor changes in risk profiles and to become less dependent on ratings agencies in evaluating credit risk.

Although governments and regulators are pressing banks to increase their lending activities to both consumers and businesses, banks have been hesitant to do so. The shortage of reliable funding sources is one aspect of banks' reluctance to lend, but a related factor involves the need for accurate risk assessments. During long periods of economic uncertainty, banks are not comfortable with their own ability to accurately assess risk. Because banks watched the proportion of nonperforming loans increase throughout the second half of 2008, their hesitancy to continue lending is not surprising.

For banks to strive and thrive in economic turbulence, they must improve their current underwriting capabilities now (no matter how low in volume) and apply advanced analytics throughout the loan life cycle, to final payoff or collections and recovery. The economy will not remain in its current state. As government stimulus packages take effect and consumers' confidence returns, banks will face a pent-up demand for new borrowing. Therefore, they should be examining the processes involved in assessing risk across the life cycle of a loan and revising them as appropriate.

## Operational Efficiency

Frequently, banking operations' disparate groups or work units are dispersed throughout the institution. Financial services companies have heavily invested in back-office applications, and silos of host-based applications are blocking the shared 360° view of customer data. Gaining additional efficiencies from these situations is not a simple task, and no single business strategy can solve all issues involved in improving efficiency. Yet it is because the challenge is so complex that banks must allocate time and effort to address it.

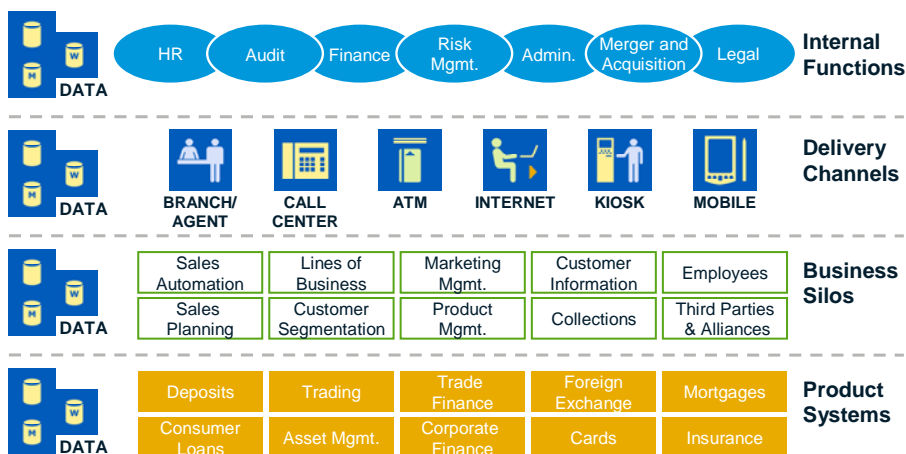
Banks can improve business efficiency and provide significant cost savings by moving customer knowledge and processes to the front end, where the customer interaction takes place. As noted earlier, collaborative customer knowledge is predicated on a shared 360° view of customer data that is available wherever and whenever it is needed. Simply having shared access to customer data brings increased efficiency to all back-office personnel and customer-facing personnel, whether they are involved in sales or in service.

Many banks' efforts to migrate to a more flexible, service-oriented architecture are still in their early stages. As a result, valuable information, particularly customer information, is not available on demand to customer-facing personnel. For example, banks routinely allow their lines of business to operate dedicated call centers for customer service. Customers who have more than one relationship with an institution are easily frustrated when trying to interact with the bank. Exhibit 4 is an overview of the siloed nature of data that is all too common in banks today.

Exhibit 4



## Bank Architecture Compounds the Difficulty of Leveraging Enterprise Data



Source: TowerGroup

As the exhibit shows, banks have developed an information architecture that is oriented to lines of business, products, or functions. These information silos have evolved over time to match the evolution of the banking business but have done so to the detriment of consumers.

As banks work to weather the current economic crisis and position themselves for the inevitable rebound in the economy, they need to keenly examine their people, processes, and technology. For an organization to strive and thrive, people (both employees and customers) must have timely access to pertinent information. As for technology, customers will embrace self-service delivery systems more completely when the information and functionality are more responsive to their needs. Therefore, many banks must explicitly invest in the technologies and platforms that enable front-end, customer-facing interactions. Finally, banks must adopt a discipline for business process management that encourages the automation of manual processes as well as the ongoing scrutiny of existing processes for efficiency.

Over the past 18 months, banks worldwide have witnessed a worrying deterioration in their efficiency ratios. In the coming 18 months, banks will face an enormous set of challenges in improving the efficiency of their business operations. TowerGroup believes that institutions will meet those challenges by revisiting major decisions related to corporate performance. They will

strive to excise costs by consolidating applications and platforms, promoting self-service technologies, and adopting alternative delivery models such as software as a service (SaaS).

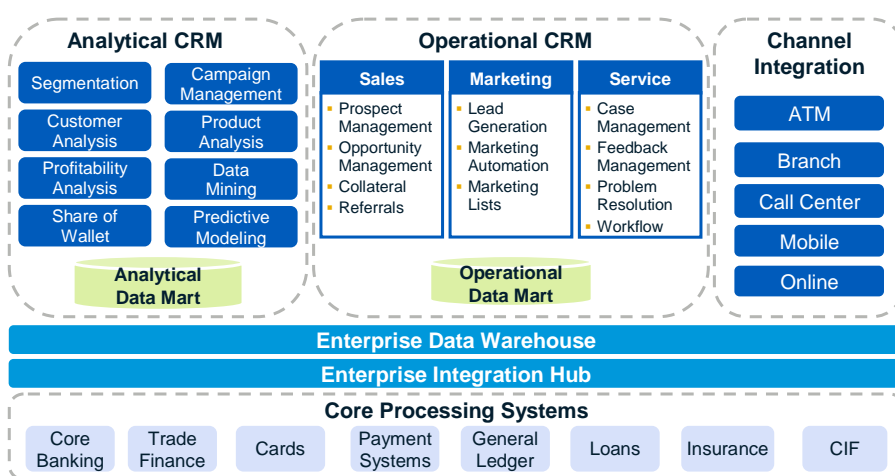
## Technology Requirements for Collaborative Customer Knowledge

As it relates to technology, collaborative customer knowledge depends heavily on the coordination of analytical CRM solutions, operational CRM solutions, and channel integration. Exhibit 5 provides an overview of these three pillars and their main points of integration. As shown in the exhibit, each pillar rests on an enterprise-wide, shared repository of customer data. This shared repository represents the 360° view of customer data and also acts as the primary source of customer data for the sales, marketing, service, compliance, and credit management processes throughout the bank. None of the three pillars is a monolith; each one is composed of additional technology tools and solutions. For collaborative customer knowledge to be operative, financial institutions need to orchestrate the workings of these multiple technologies.

Exhibit 5



### Collaboration in Customer Knowledge: An Integrated Approach Across the FSI



Source: TowerGroup

As banks adapt their business models to focus more on customers, a coincident alteration in IT investment strategy occurs. TowerGroup believes that banks will continue to shift IT investments from back-end, host-based applications to front-end and desktop applications that impact customers directly at the points of customer interaction. As an example, financial planning applications that have traditionally been host-based, back-end systems are now moving to the front office to ensure adequate access for customer-facing staff and to enable greater and more convenient collaboration with customers.

### ***Analytical CRM***

The major technologies that make up the analytical CRM pillar include those that allow an institution to derive customer knowledge from what would otherwise be raw customer data. Once the relevant customer data is pulled into the analytical data mart, the institution can apply a variety of analytical tools, including predictive modeling and data mining, to create their analysis of customer segmentation, profitability, share of wallet, and product usage. Of particular value to banks is the ability to understand what products and services a customer will be most receptive to at any given time. Creation of sales prompts is increasing in importance to banks of all sizes. They can then use campaign management software to create complex marketing campaigns and to map appropriate strategies related to offers, channels, and messaging for customers.

### ***Operational CRM***

The operational CRM pillar supports business applications that enable sales, service, and marketing functions, which are the ones most commonly associated with the acronym CRM. Each of these business functions plays a critical role in enabling an institution to strive and thrive over the next five years. Appropriately managing prospects, referrals for existing customers, and other opportunities is a clear priority for banks. Similarly, they must properly manage leads and marketing lists to ensure that sales and marketing functions are working in harmony. Finally, banks must quickly and accurately attend to the service needs and requests from consumers and integrate problem resolution with feedback management to ensure that bank policies, procedures, and processes are in sync with bank strategy.

### ***Channel Integration***

The final pillar, channel integration, includes the principal points of interaction between the institution and customers. The five major delivery channels — ATM, branch, call center, mobile, and online — must be sufficiently integrated so that customers can switch among them without degradation in information quality or consistency of service. Thus, a simple inquiry for an account balance must render the same answer regardless of the channel used. Today, customers tend to use multiple delivery channels for everyday transactions, depending on their personal idea of convenience, quality of service, security, and cost. As a result, banks must make account information available to all the channels consistently (self-service and staffed), and customer information captured in one channel must be available to all other channels.

### ***Three Pillars in Concert***

Collectively, the three pillars of technology form the basis for collaborative customer knowledge. The rationale for the descriptions is based on the critical strengths represented in each pillar. For example, channel integration enables consistent and “close-to-frictionless” interactions between the institution and the customer or prospect, yet the analytical CRM pillar determines the communication strategy. Finally, it is the operational CRM pillar that ensures the quality of the interaction. Taken in concert, these three pillars facilitate high-quality interactions between the institution and customers, regardless of the channels that customers prefer.

## Conclusion

Customer data and customer knowledge are perhaps banks' most undervalued and underleveraged corporate assets. The inability to use them has fundamental impacts on a bank's ability to retain customers, increase share of wallet, manage risk effectively, and drive process efficiencies. For banks to succeed over the near term, their managers across the enterprise must be committed to actively leverage data and engineer a technology infrastructure that facilitates dynamic collaboration.

When banks employ customer knowledge collaboratively, they empower both customer-facing personnel and customers as they use self-service technologies. Collaborative customer knowledge relies on integrated customer relationship management (CRM) capabilities that optimize sales, service, and marketing functions through the application of advanced analytics and seamless distribution via channel integration. Creating this technology environment across an institution has long-lasting benefits, not the least of which is an enhanced understanding of existing customers' needs and expectations.

As banks seek to leverage their customer data more fully and truly enable a collaborative environment, the most frequent stumbling block is access to the applications and data repositories they need to create the true 360° view of the customers. In far too many institutions, customer knowledge resides in single-purpose data marts within business units. Initiatives for customer sales, service, and marketing are hampered, and customers' satisfaction with both self-service and staffed delivery channels declines. Given the challenges of the current economic climate, no institution can afford *not* to pursue holistic and collaborative customer knowledge.

While banks adapt their business models and strategies to be more customer focused, they are also shifting their IT investments from back-end host-based applications to front-end desktop applications. Banks are focusing IT investments at the points of customer contact. The practical implications of this type of alteration in IT spending strategy include the realization of sales, service, and process efficiencies for consumers and staff alike.

TowerGroup believes that over the next few years, financial institutions have a business imperative to invest in a new CRM platform that will allow them to leverage existing applications and investments to gain customer and business insight, scale, self-service capabilities, and process efficiency. Institutions will make the investment despite economic uncertainty. Integration of CRM capabilities is a first step in this journey. Embracing this mandate will allow banks to differentiate themselves effectively from their peers and position themselves for the inevitable economic recovery.



*Microsoft commissioned TowerGroup to conduct independent research and analysis of data management practices and trends in financial services. The content of this report is the product of TowerGroup and is based on independent, unbiased research not tied to any vendor product or solution. Although every effort has been made to verify the accuracy of this information, neither TowerGroup nor the sponsor of this report can accept any responsibility or liability for reliance by any person on this research or any of the information, opinions, or conclusions set out in the report.*

## About Microsoft Dynamics

Microsoft Dynamics is a line of integrated, adaptable business management solutions that enables you and your people to make business decisions with greater confidence. Microsoft Dynamics works like familiar Microsoft software, such as Microsoft Office, which means less of a learning curve for your people, so they can get up and running quickly and focus on what's most important. Built to work with Microsoft technologies, it works easily with the systems your company already has implemented. By automating and streamlining financial, customer relationship, and supply chain processes, Microsoft Dynamics brings together people, processes, and technologies, helping increase the productivity and effectiveness of your business and helping you drive business success.

Worldwide 1-701-281-6500

United States and Canada, toll free, 1-888-477-7989

[www.microsoft.com/dynamics](http://www.microsoft.com/dynamics)

The information contained in this document represents the current view of Microsoft Corporation on the issues discussed as of the date of publication. Because Microsoft must respond to changing market conditions, this document should not be interpreted to be a commitment on the part of Microsoft, and Microsoft cannot guarantee the accuracy of any information presented after the date of publication.

This White Paper is for informational purposes only. MICROSOFT MAKES NO WARRANTIES, EXPRESS, IMPLIED, OR STATUTORY, AS TO THE INFORMATION IN THIS DOCUMENT.

Complying with all applicable copyright laws is the responsibility of the user. Without limiting the rights under copyright, no part of this document may be reproduced, stored in or introduced into a retrieval system, or transmitted in any form or by any means (electronic, mechanical, photocopying, recording, or otherwise), or for any purpose, without the express written permission of Microsoft Corporation. Microsoft may have patents, patent applications, trademarks, copyrights, or other intellectual property rights covering subject matter in this document. Except as expressly provided in any written license agreement from Microsoft, the furnishing of this document does not give you any license to these patents, trademarks, copyrights, or other intellectual property.

© 2009 Microsoft Corporation. All rights reserved. Microsoft, Microsoft Dynamics, and the Microsoft Dynamics logo are registered trademarks or trademarks of Microsoft Corporation in the United States and/or other countries. The names of actual companies and products mentioned herein may be the trademarks of their respective owners.