Deloitte.

Bricks and clicks

Mapping the future of branches

Key points

- Deloitte's research has analysed over 10,400 bank and building society branch locations in England and Wales. We found that more than half of the total branch network is positioned in micro-markets where demand for high-quality branch services is likely to increase in the next five years.
- Nearly one-quarter of the branch network covers markets where older people, and not younger people, are likely to create the biggest disruption by shifting to direct banking channels, including the Internet and mobile.
- In today's diverse and dynamic retail financial services market, banks and building societies need to combine their thinking on micro-markets and multi-channel strategy to ensure they can meet their customers' needs for convenience, service and value.

Contacts

Louise Brett
Partner, Financial Services Analytics Leader
+44 (0)20 7303 7225
lbrett@deloitte.co.uk

Harvey Lewis
Head of Analytics Research
+44 (0)20 7303 6805
harveylewis@deloitte.co.uk

Margaret Doyle
Head of Financial Services Research
+44 (0)20 7007 6311
madoyle@deloitte.co.uk

Zahir Bokhari
Partner, UK Banking Leader
+44 (0)20 7303 5337
zbokhari@deloitte.co.uk

Stephen Williams
Partner, Building Societies Leader
+44 (0)113 292 1231
stephenwilliams@deloitte.co.uk

Sulabh Soral
Senior Manager, Predictive Analytics Centre of Excellence
+44 (0)20 7007 2123
ssoral@deloitte.co.uk

Analytics Applied.

Powered by Deloitte Analytics

Contents

Authors

Louise Brett
Partner, Financial Services Analytics Leader
+44 (0)20 7303 7225
lbrett@deloitte.co.uk

Harvey Lewis
Head of Analytics Research
+44 (0)20 7303 6805
harveylewis@deloitte.co.uk

Sulabh Soral
Senior Manager
Predictive Analytics Centre of Excellence
+44 (0)20 7007 2123
ssoral@deloitte.co.uk

Neal May
Manager
Consulting
+44 (0)20 7303 7009
nemay@deloitte.co.uk

Foreword

Welcome to this Deloitte Analytics report investigating the forces of change on today's retail bank and building society branch networks.

After more than a decade of rationalisation, branch networks are still ill-placed and ill-equipped to meet the needs of their customers in the digital age. Conventional wisdom suggests that the increasing use of direct channels by a growing online and mobile population makes the branch nothing more than a costly relic of an analogue era.

Deloitte's view, however, is that branches will remain key to the success of retail banking institutions. Consumer surveys conducted in 2002 and 2007, reported in *Bring back the branch* and *Winning with branches*, suggested that branches were the only practical focal point for banks and building societies to deliver the right mix of convenience, service and value to customers.[1,2] The sixth edition of Deloitte's Consumer Review, *Reinventing the role of the high street*, published in November 2013, reinforces this view: consumers said they were seeking an integrated shopping experience and expect retailers to deliver it consistently across all channels – digital and physical.[3]

Approached in the right way, the high street represents a new opportunity for Britain's banks and building societies to create the integrated multi-channel environment they aspire to. But profound shifts in local economic conditions, personal wealth, population demography and the business environment over the next few years make the micro-market picture very complex. What is the extent to which this tapestry of change will impact branches? Using a wide array of open data and commercially licensed data for England and Wales, explored with advanced analytics, this is the question our research has addressed.

Our findings suggest that branches are indeed poised for a renaissance – but perhaps not in their current numbers or formats. At one end of the spectrum, the branch needs to become a simple, convenient gateway to more direct channels so customers can self-serve; in other formats, branch staff need to shift their focus from routine over-the-counter cash transactions to providing a tailored, informed and personal service for new and existing customers on the hunt for competitively priced financial products. Understanding branch micro-markets is the essential first step towards creating the ideal network footprint and significantly reducing cost-to-income ratios.

We'd like to thank the many organisations that made their data available for this analysis. We hope that you find our insights thought-provoking and useful, and welcome your feedback. Thank you for your interest.

Louise Brett

Louise Brett
Partner, Financial Services Analytics Leader

Death by digital?

The branches of Britain's once-thriving bank and building society networks are under attack. Despite new growth in the economy, operating costs are rising and revenues have stagnated.

The damage is significant, according to the campaign for Community Banking Services (CCBS). In the last ten years, 2,153 bank branches in Britain, including branches of converted building societies, have closed.[4] What was already one of Europe's lowest density branch networks now retains only 180 branches per million customers.[5]

The harsh reality is that branches have not kept up with the times. For decades, people visited the branch for credit approval, to conduct transactions, learn about products and services, and for customer service. They may have once been at the heart of the high street but branches seem much less relevant in today's digital world. Customers now expect much greater convenience and want banking services delivered through a seamlessly integrated set of telephone, web, mobile, Automated Teller Machine (ATM), remote and in-person channels wherever they may be. They are more price-sensitive and less loyal than ever before.

To add to the pressure, regulators have recently tightened up the rules on the provision of advice to customers and are fostering new rules to make it easier for customers to switch accounts. They are likely to want a say in any future decisions on branch locations, too.[6]

From the bank or building society's perspective, some customers carry more risk than others, which is something retail financial institutions are now more attuned to. As a consequence, the search for new and profitable customer segments is proving increasingly difficult and thus the cost to serve customers in branches is rising. In the face of seemingly insurmountable change, banks and building societies are understandably seeking to rationalise.

But does digital's relentless advance really sound the death knell for branch networks? Or do the increasingly diverse and dynamic markets surrounding branches reveal alternative strategies that help financial institutions balance footprints and formats more effectively?

The harsh reality is that branches have not kept up with the times. For decades, people visited the branch for credit approval, to conduct transactions, learn about products and services, and for customer service.

Banks and building societies that are able to understand this 'new normal' are going to be better placed to hedge the risk associated with market dynamics, and provide more innovative, tailored and higher-quality retail financial services.

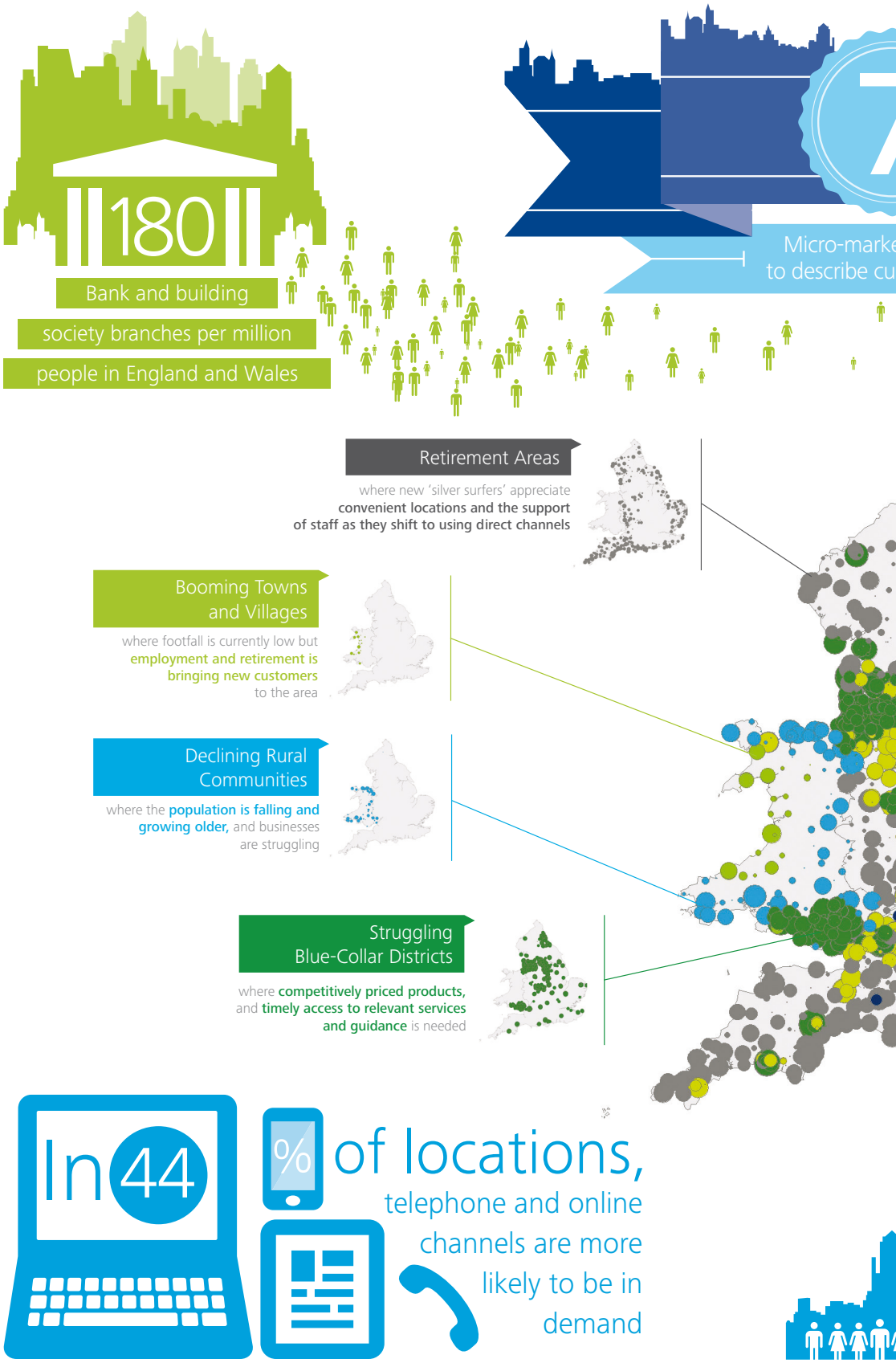
To answer this question, Deloitte characterised the markets surrounding more than 10,400 branches for nearly 100 retail bank and building society brands.[7] The analysis included calculating retail and business banking customer flows using gravity modelling.[8] All branches were then segmented using 56 variables, including current and forecast changes in consumer behaviour, age structures, personal wealth, economics and business demography. More information on the methodology used can be found in the Appendix.

As illustrated in Figure 1, the research found that branches fall into seven key micro-market segments. Fifty-six per cent of the total branch network in England and Wales is positioned in segments where demand for high-quality branch services may be likely to increase rather than decrease in the next five years. Furthermore, the research suggests that nearly one-quarter of the branch network covers micro-markets where older people, and not younger people, are likely to create the biggest disruption by shifting to direct banking channels, including web and mobile.

As the recent Grimsey Review of the high street suggested, "One thing is certain. The high street landscape has now irrevocably changed and there is no point clinging on to a sentimental vision of the past. We have to start planning for a bold new world".[9]

Banks and building societies that are able to understand this 'new normal' are going to be better placed to hedge the risk associated with market dynamics, and provide more innovative, tailored and higher-quality retail financial services.

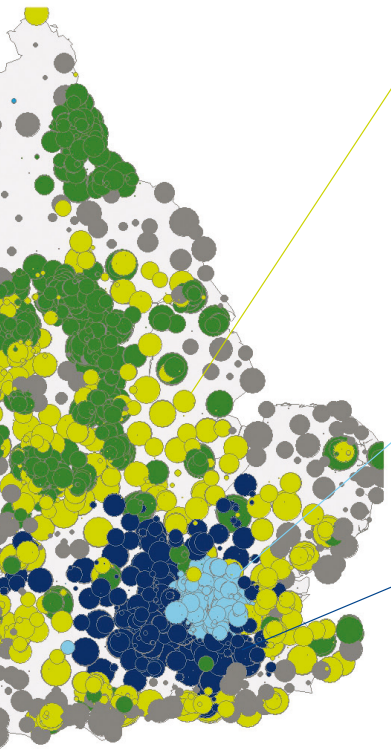
Figure 1. Mapping the future of branches in England and Wales

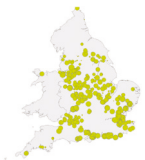


Source: Deloitte analysis

72%

of consumers said that they still go to the high street to access banking and financial services





Traditional Urban Centres

where students, job seekers and house hunters need a blend of **convenience and no-nonsense guidance** to help them take their first steps towards financial independence

Super Conurbations

where a new type of young, affluent customer is seeking a mix of contemporary formats, **convenience and personal service** to guide them through new product purchases

Commuter Zones

where wealthy workers and their families need branch **flexibility and an efficient, tailored service** to suit their busy schedules

In 56%

of locations, branches are more likely to be in demand

The seven types of micro-market

This research has identified seven different types of branch catchment based on an analysis of a range of static and dynamic micro-market factors. These factors have been selected because they drive consumer and business banking demand and channel usage, and thus influence not only branch footprint but also formats. The model also includes both retail centre information and business demography to account for some of the differences between resident populations and daytime populations that occur particularly in urban areas.

The seven segments identified are:

- Super Conurbations
- Commuter Zones
- Retirement Areas
- Booming Towns and Villages
- Declining Rural Communities
- Struggling Blue-Collar Districts
- Traditional Urban Centres.

Collectively, these seven segments paint a broad picture of the branch banking environment in a given area. For instance, population demographics and personal wealth drive the take-up of financial services and products and, in conjunction with data on Internet penetration and online banking, provide some insight into customers' preferred choice of channel.

The presence of different types of retailer and small businesses drives additional footfall and demand for over-the-counter transactions in branches. And coupling personal wealth with other economic factors, such as the affordability of local housing and worker productivity, gives us a bearing on the types of products likely to be in demand and their apparent affordability.

These segments are not intended to replace the segments that banks and building societies typically rely upon to understand customer value; instead, they provide a rich market insight layer to complement existing analyses and act as an important precursor to network optimisation.

This section examines the defining characteristics of the seven types of micro-market and considers their impact in terms of customer convenience, service and value.

The dynamic factors in this analysis are based on projections of their respective static factors for the next five years and are measured by the total cumulative percentage change that occurs over the future period.

Super Conurbations

These micro-markets are predominantly in the Greater London area. The people who live here are typically young, skilled workers aged between 25 and 44.

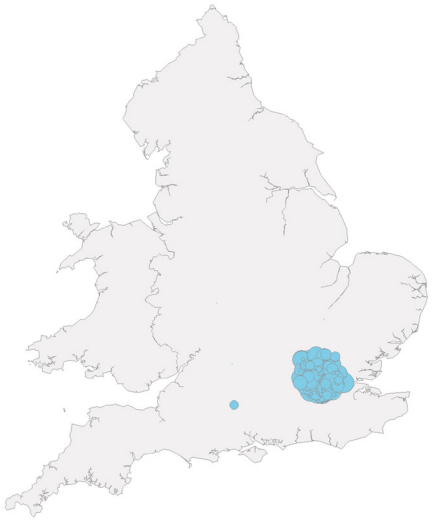
Even though this segment is the country's wealthiest and workers here are among the most productive, incomes and expenditure are not expected to increase significantly in the next five years. House prices are very high and accelerating at the fastest rate nationally, and rents are also increasing.

Business is booming in these areas, too. Retailers, hotels, restaurants, landlords and property management firms are all moving in – in greater numbers than anywhere else in the country.

The relative youth of the people who live in these catchments suggests that they are much more likely than average to use telephone, Internet or mobile banking for their day-to-day transactions – or even for purchasing some simple products.

However, the primary objective of branches in this segment should be customer acquisition. Young customers will be on the hunt for competitive products, particularly mortgages, savings and investments and pensions, from relevant brands.

Figure 2. Catchments in Super Conurbations
Circle size is proportional to the total number of branches and retail outlets in the catchment



Source: Deloitte analysis

And their interest may be fuelled not only by effective branch marketing but also by references from their employers with whom the banks and building societies may already have a relationship – and business density is especially high in Super Conurbations. Branches thus play a key role in acquisition. They need to provide a fresh, contemporary format to attract customers, with sufficient meeting space allocated to provide a personal and friendly service.

Although they may not be the most valuable now, these young customers potentially have significant lifetime value. Thus, banks and building societies should focus on fast-tracking them through purchases of anchor products and maintaining the quality of service as they progress in their careers locally or elsewhere.

Branches in these micro-markets are also likely to be the busiest in the country. They will see the highest levels of footfall from individual consumers and small businesses, particularly at peak times of the working day. Convenient locations are therefore important, as are low cost and efficient counter services to retain existing customers.

Key statistics

346,300
Average size of catchment population

37 years
Average age

+9%
Change in size of population

£28,600
Average disposable income

£334,000
Average house price

-20%
Change in unemployment rate

14%
Change in number of businesses

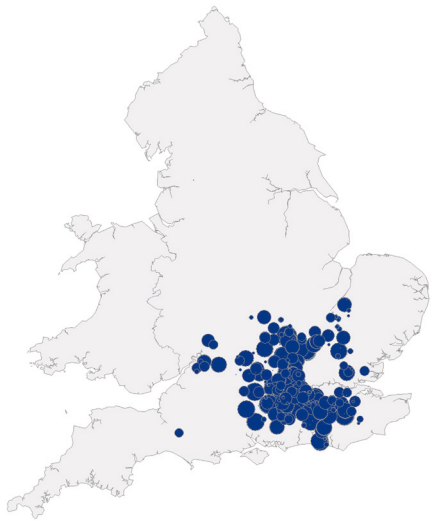
Commuter Zones

These micro-markets are predominantly in London's rural and suburban commuter belt, and include prosperous towns and cities, such as Bristol, Reading, Oxford and Guildford. The people who live in these leafy suburbs are a mix of young and mature families; they are also among the country's most affluent and they are getting wealthier.

House prices in these micro-markets are rising quickly, although many people already own their own home – either outright or with a mortgage. People spend more money here, too, and both income and expenditure are increasing at the fastest rates in the country. Consequently, high streets and shopping centres in these micro-markets are bustling, with many big brand retailers present.

In the local economy, unemployment is falling sharply, driven by strong growth in the number of businesses of all sizes forecast to locate here.

Figure 3. Catchments in Commuter Zones
Circle size is proportional to the total number of branches and retail outlets in the catchment



Source: Deloitte analysis

Branches in Commuter Zones should focus on both customer acquisition and retention. Acquiring new high-value retail customers may be hard given that many people normally resident in this segment will travel to elsewhere to work. However, steady growth in the number of businesses here may also drive inward migration and an attractive cohort of potential new customers.

On the whole, customers are likely to appreciate extended or non-standard opening hours that match their busy working and domestic schedules. They will also place more value on an efficient and personal service rather than the availability of competitively priced anchor products.

Peak footfall is most likely to occur at weekends or either side of the daily commute. The highest footfall is likely to be near major transport hubs or on busy high streets and in shopping centres.

Branches here may see greater than average interest in family products, such as wills, life insurance and other types of insurance cover, which have typically not been part of the branch banking product portfolio.

Key statistics

45,700
Average size of catchment population

40 years
Average age

+7%
Change in size of population

£30,200
Average disposable income

£305,000
Average house price

-22%
Change in unemployment rate

+5%
Change in number of businesses

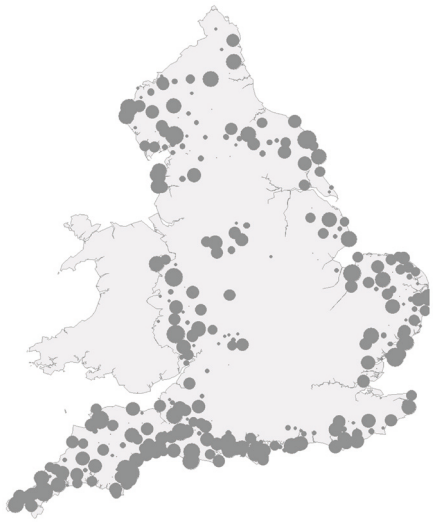
Retirement Areas

These micro-markets are typically coastal or in rural locations far away from the hustle and bustle of the city. The highest densities of branches in this segment are in the counties of Dorset, Somerset, Devon and Cornwall, and include towns such as Bournemouth and Weymouth. The average age of the people who live here is higher than the national average and the proportion of the population aged 16 to 24 is very low.

People in these catchments do not have a lavish lifestyle. Although many own their own homes outright, incomes from pensions and employment are typically low. However, income and expenditure are set to grow at the fastest percentage rates of any of our segments as more affluent people relocate to Retirement Areas when they stop work.

The economy in these micro-markets is largely driven by tourism, and there are relatively few large businesses. Unemployment is lower than average but is rising quickly, perhaps as the number of businesses in the area shrinks and people of working age choose to retire early rather than remain in work.

Figure 4. Catchments in Retirement Areas
Circle size is proportional to the total number of branches and retail outlets in the catchment



Source: Deloitte analysis

Branches here face a quandary: small-business custom is likely to be low and older retail customers are much less likely than average to want to purchase new financial products at their mature life-stage. However, many customers still want to come into branch to carry out day-to-day cash transactions as they always have done, typically later in the day and when they are also visiting other local shops and amenities.

But does this mean that customers need branches to retain their existing footprints and formats? Not necessarily. This is because older people are turning to digital channels in ever-greater numbers. Indeed, Internet use and online banking in Retirement Areas is growing at one of the fastest rates.

Therefore, retail financial institutions in this segment need to educate customers and help them to make the switch from physical to digital services. And as demand for bricks-and-mortar services starts to wane, branches need to adopt a system of easy-to-use self-service tools in-branch, integrated with web applications tailored for these new 'silver surfers'.

Key statistics

22,200
Average size of catchment population

45 years
Average age

+5%
Change in size of population

£23,600
Average disposable income

£209,000
Average house price

+28%
Change in unemployment rate

-4%
Change in number of businesses

Booming Towns and Villages

The small numbers of micro-markets in this segment are all in West Wales, in towns such as Aberystwyth and Cardigan. People here are, on average, among the oldest in the country and the population is ageing at the fastest rate. Surprisingly, though, the population is also growing fast – across all age bands. Even though the total number of businesses is falling, medium-sized employers are starting to move in, attracting new jobs and a younger workforce into the region. The number of restaurants and hotels is also increasing but retail businesses are struggling, as are very small businesses.

Unlike in Retirement Areas, though, people in Booming Towns and Villages have the lowest levels of disposable income and expenditure across the country, and neither is expected to increase significantly over the next five years.

Branches in these locations may have been struggling with low customer numbers and high cost-to-income ratios historically, but an influx of new businesses and employees coupled with an ageing population demands a fresh look at footprint and formats.

Value is likely to be a driving factor that attracts new customers in this segment, as is a mix of formats that provide a sensible balance between cash transactions and space for product guidance and interviews.

The high rates of change in some variables for this segment suggest that micro-market conditions are still evolving. And, even though the segment is small, as conditions stabilise in the future, some branches may need to be subsumed into other segments whose characteristics are ultimately more similar.

Figure 5. Catchments in Booming Towns and Villages
Circle size is proportional to the total number of branches and retail outlets in the catchment

Source: Deloitte analysis

Key statistics

15,500
Average size of catchment population

44 years
Average age

+30%
Change in size of population

£19,800
Average disposable income

£162,000
Average house price

-2%
Change in unemployment rate

-5%
Growth in number of businesses

Declining Rural Communities

This segment includes the rest of Wales, in towns such as Milford Haven and Abergavenny. The people living here are among the country's poorest. Most noticeably, though, the populations of the micro-markets in this segment are in decline. For example, substantial falls are forecast in the number of over-45s, as experienced workers move out of the area in search of jobs.

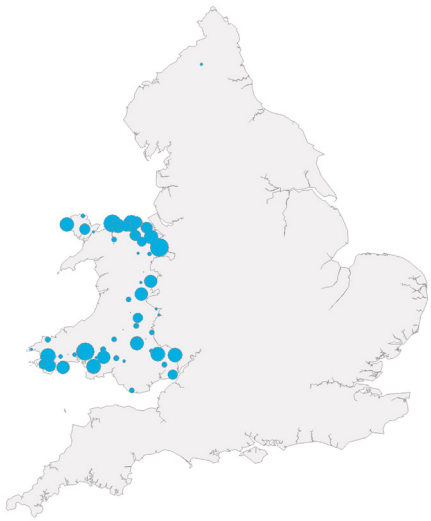
The signs of the decline can be seen in the local economy, too, with unemployment set to remain high due to large projected falls in the number of retail and very small businesses. And, although the numbers of larger businesses are forecast to increase in the next five years, this is from a very low base. Retail centres in these locations are not likely to be faring well, either, with many outlets closing.

Like many other types of retailer, branches in these areas are likely to be struggling with shrinking footfall and reduced demand for financial products and services.

Cost-efficiency will be the key to survival here, driven by streamlined services for cash transactions and easy access to remote and online services provided in the branch. Co-locating with other retailers will help to shrink square footage and reduce costs while improving convenience for customers.

There are also bigger questions, such as how should the bank work with and support the local population in Declining Rural Communities to spearhead the return of growth, and to help these towns and villages get back on track?

Figure 6. Catchments in Declining Rural Communities
Circle size is proportional to the total number of branches and retail outlets in the catchment



Source: Deloitte analysis

Key statistics

22,200
Average size of catchment population

43 years
Average age

-1%
Change in size of population

£21,500
Average disposable income

£161,000
Average house price

0%
Change in unemployment rate

-6%
Change in number of businesses

Struggling Blue-Collar Districts

This segment is dominated by towns and cities in the north of England and also in Wales, such as Liverpool, Newcastle and Cardiff. And while other segments may be attracting a younger and more affluent population – and thus potentially valuable customers – the micro-markets in Struggling Blue-Collar Districts are under pressure.

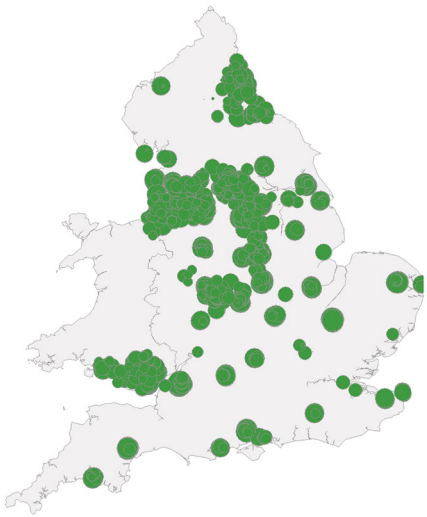
Unemployment in these areas is higher than in any of our other segments although it is falling. As a consequence, the people living here do not have as much disposable income as those in other segments, and they spend less, too. And unlike the towns and cities farther south, the housing market in these areas is depressed. House prices in this segment are still forecast to increase in the next five years but at the lowest rate in the country.

There are relatively high proportions of large businesses and retailers in these micro-markets, but, more broadly, although the number of small-to-medium enterprises – employing fewer than 250 people – is high at present, the number is not growing.

For branches in these segments, cash is likely to be king – driven by both the resident population and the currently high proportion of small-to-medium enterprises. The high levels of unemployment and low levels of consumer expenditure are unlikely to drive significant demand for investment products. Instead, customers may be seeking help to manage debt on credit cards, or to restructure loans and mortgages. Affordable anchor products with benefits, such as insurance or cash-back, may therefore be of great interest.

Innovation in this segment is very important to reduce the cost to serve. Re-aligning formats so that a greater proportion of branches provide simple, highly efficient transaction services, while a small number of conveniently located hubs provide financial guidance and product support, is likely to improve cost-to-income ratios. In particular, branches in proximity to or co-located with other retailers are likely to score high on the convenience scale while reducing operating costs.

Figure 7. Catchments in Struggling Blue-Collar Districts
Circle size is proportional to the total number of branches and retail outlets in the catchment



Source: Deloitte analysis

Key statistics

106,800
Average size of catchment population

40 years
Average age

+5%
Change in size of population

£21,200
Average disposable income

£151,000
Average house price

-8%
Change in unemployment rate

-3%
Change in number of businesses

Traditional Urban Centres

These micro-markets are mostly in the centres of busy towns and cities of England and Wales, such as Portsmouth, Bristol and Manchester. The people who live here are currently close to the national average in age and wealth.

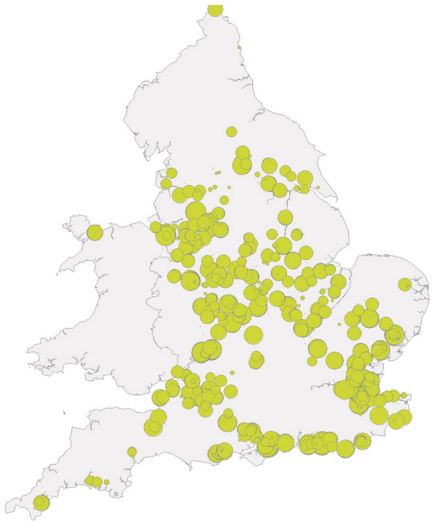
Unemployment in these areas is also average but is falling quickly, driven by solid growth in the number of small to medium-sized businesses. Although personal incomes and expenditure may be modest, both are set to increase at above the national rate. For branches in this segment, this means that attracting new, young customers is as crucial as retaining more mature, existing customers.

The challenge for branches, therefore, is not only to attract new customers with competitive rates and other offers, but also to build a long-term relationship through high-quality, tailored services, particularly with students arriving in the university towns and cities in this segment who may subsequently migrate to other areas for their future careers.

For these customers, the quality and ease-of-use of direct channels are also going to be important factors when it comes to choosing a bank brand. Potentially, the first-time home buyers in this younger sub-segment face a much less challenging environment than in Super Conurbations because the ratio of average house prices to incomes is much lower.

And although the remainder of the local population and large numbers of local consumer-facing businesses will drive high footfall volumes and over-the-counter transactions, branches should consider how they can streamline their formats to continue providing a superior service for existing customers while simultaneously creating sufficient capacity to focus on attracting and retaining new customers.

Figure 8. Catchments in Traditional Urban Centres
Circle size is proportional to the total number of branches and retail outlets in the catchment



Source: Deloitte analysis

Key statistics

55,300
Average size of catchment population

41 years
Average age

+6%
Change in size of population

£24,100
Average disposable income

£202,000
Average house price

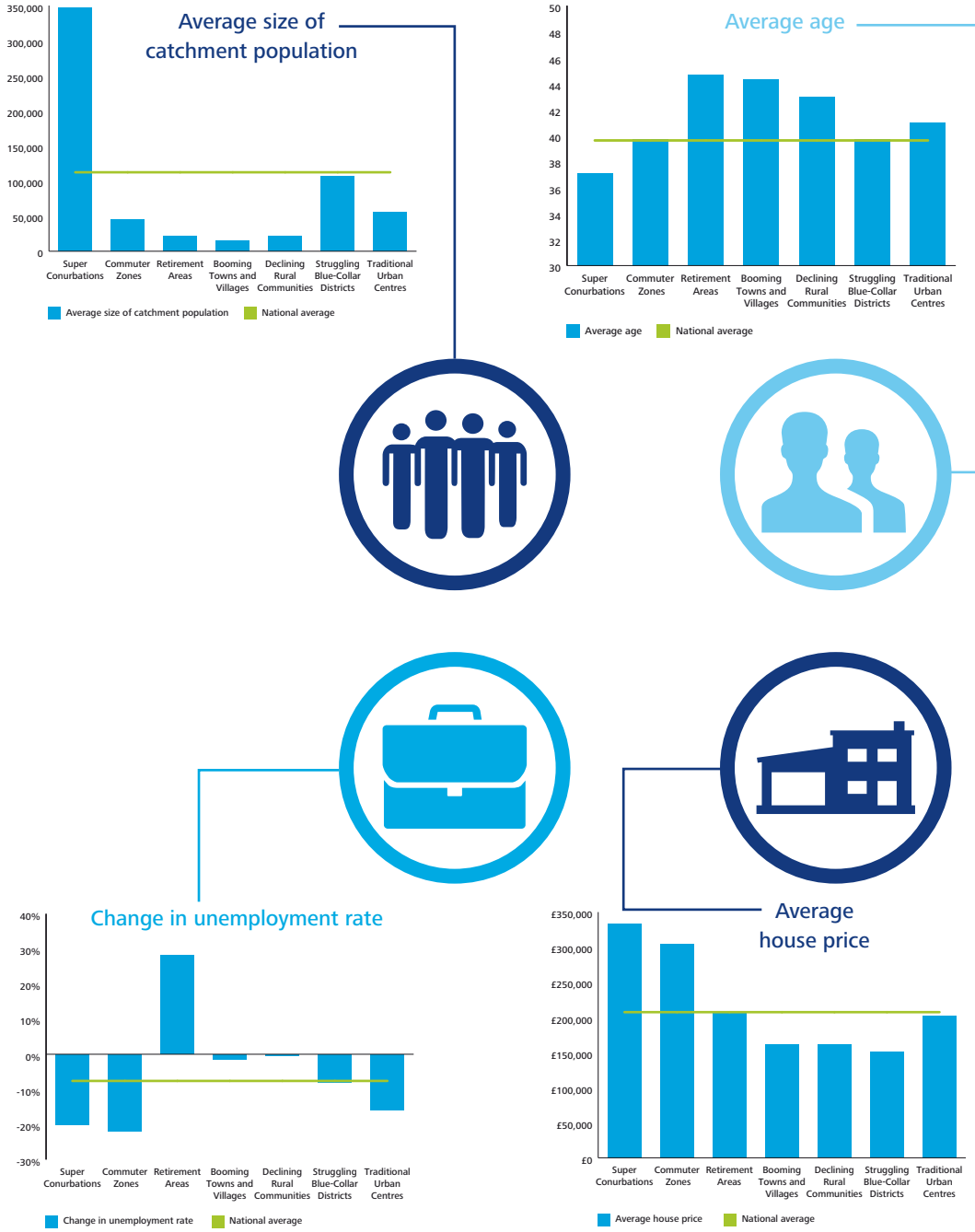
-16%
Change in unemployment rate

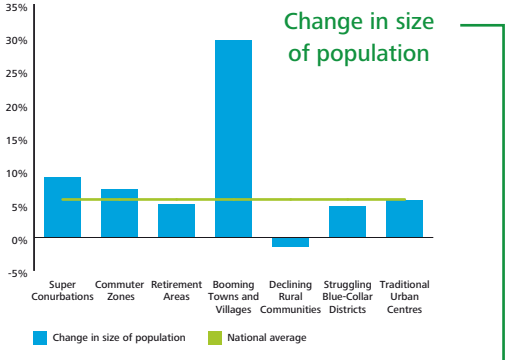
0%
Change in number of businesses

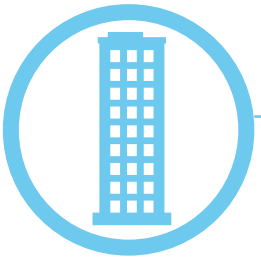
Segment comparison

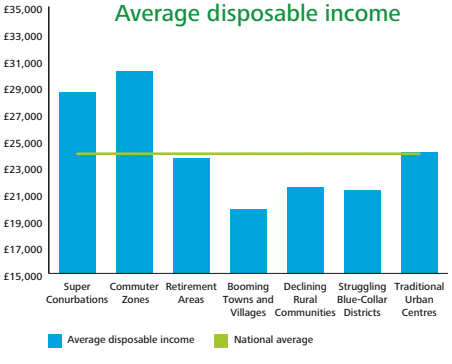
The variation of key statistics across the seven micro-market types is shown in Figure 9.

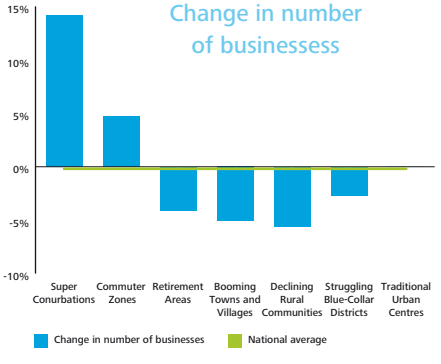
Figure 9. Differences in the key statistics describing the seven types of micro-market




Change in size of population
35%
30%
25%
20%
15%
10%
5%
0%
-5%
Super Conurbations
Commuter Zones
Retirement Areas
Booming Towns and Villages
Declining Rural Communities
Struggling Blue-Collar Districts
Traditional Urban Centres
Change in size of population
National average




Average disposable income
£35,000
£33,000
£31,000
£29,000
£27,000
£25,000
£23,000
£21,000
£19,000
£17,000
£15,000
Super Conurbations
Commuter Zones
Retirement Areas
Booming Towns and Villages
Declining Rural Communities
Struggling Blue-Collar Districts
Traditional Urban Centres
Average disposable income
National average


Change in number of businessess
15%
10%
5%
0%
-5%
-10%
Super Conurbations
Commuter Zones
Retirement Areas
Booming Towns and Villages
Declining Rural Communities
Struggling Blue-Collar Districts
Traditional Urban Centres
Change in number of businesses
National average

Population coverage

Now that the micro-market segments have been identified, banks and building societies need to understand how their branches can serve them effectively.

The first step in the analysis is to understand and contrast each brand's market share and population coverage, as shown in Figure 10, which also highlights two contrasting aspects of the 'network effect'.

Firstly, there appears to be a law of diminishing returns above approximately eight per cent branch share. Above this point, only marginal improvements in population coverage are possible even with substantial increases in branch numbers. For these banks and building societies, cost-to-income ratios will be more sensitive to the general shift in customer behaviour towards direct channels and decreasing appetite for new products.

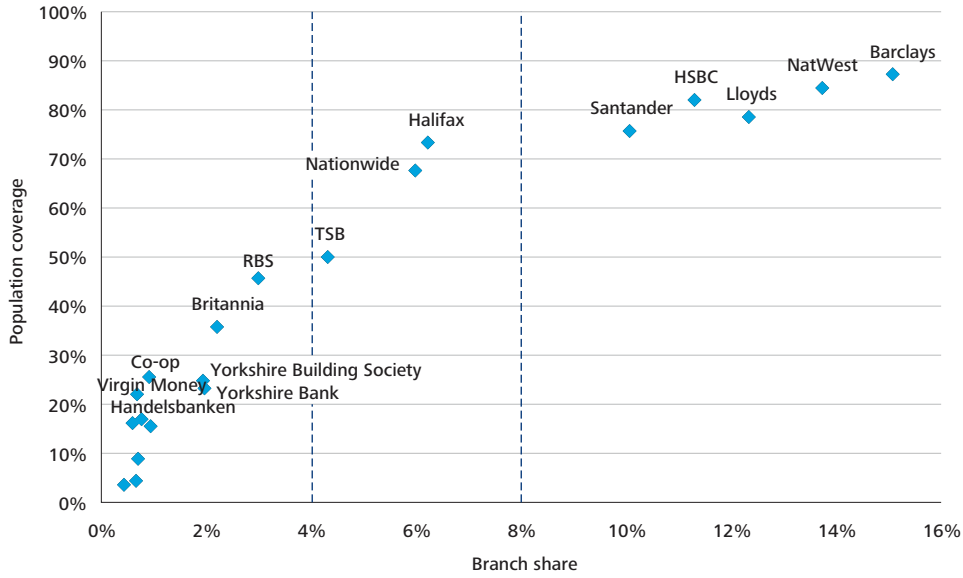
Secondly, below four per cent branch share, relatively modest branch network expansion can translate into proportionally greater increases in population coverage and potentially higher revenues.

The relationship between population coverage and branch share is particularly important for regional rather than national brands. In these cases, careful thought needs to be given to where expansion or rationalisation occurs because the majority of branches in the network are clustered together in one or a small number of areas of the country where brand awareness among customers is high.

For example, opening new branches in large towns or cities far from a brand's 'heartland' may be much less successful than the coverage would suggest because potential customers are not familiar with the brand. A balance needs to be struck between growth and regional impact.

In reality, neither branch share nor population coverage equates to increased revenue. And branch networks cover catchments of many different sizes. While some branches are located in towns or cities with large populations, others serve very small populations.

Figure 10. Population coverage for the top 20 banks and building societies in England and Wales



Source: Deloitte analysis

A key part of understanding network footprint is therefore being able to determine the likelihood that any branch in a network serves a population of a given size.

Figure 11 displays the contrasting positions of two national brands. Both networks cover a similar percentage of the population overall. However, one network spans catchments whose populations range in size from approximately 100 to 2.5 million people, with a catchment size of 25,000 people most likely. The other network, on the other hand, covers a narrower range of larger catchments. The maximum probability for this network coincides with a catchment population of approximately 40,000 people.

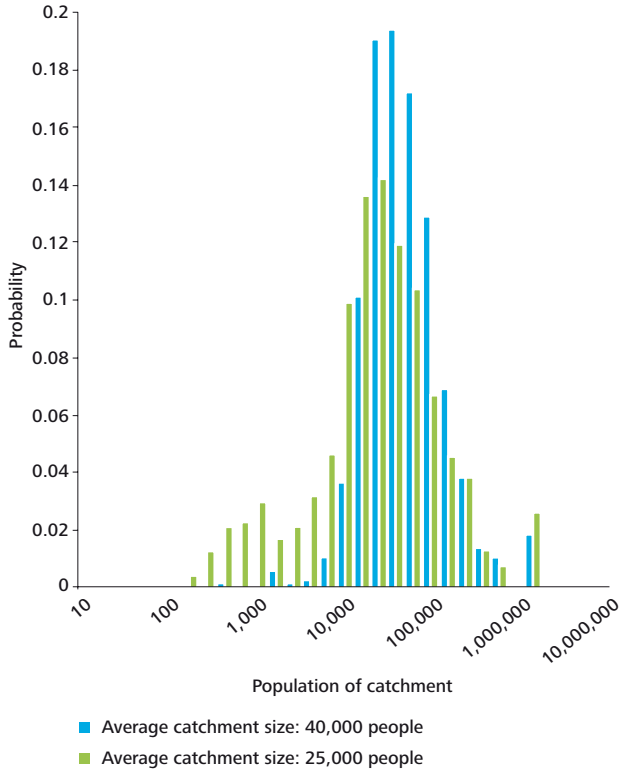
Banks or building societies whose networks share this taller, narrower distribution tend to have a higher-than-average proportion of their branches on the high streets of the country's major towns and cities. Their coverage efficiency is a double-edged sword, though, because 'lean' networks like these may have less flexibility when making cuts in branch numbers or in seeking out equivalent prime locations for expansion.

Moreover, some branches of lean networks may not have sufficient floor space or architectural flexibility to cover demand adequately, thereby impacting customer service and sales. Equally, cost-to-income ratios for small branches in minor towns or villages may be so low that they are never considered for rationalisation.

In practice, many factors influence the effectiveness of branch footprint for individual brands. Optimising a network requires more than just an analysis of catchment size.

Even without taking into account more practical constraints, such as the remaining term on a property lease or a commitment made to a small community, fundamental restructuring decisions cannot be based on population coverage or footfall estimates alone. They need to account for a range of micro-market factors associated with both internal and external conditions, such as customer demographics and wealth, the appetite of customers for purchasing new products, the disposition of local businesses and the health of the regional economy, as well as a set of risk factors.

Figure 11. Contrasting population coverage for two national brands



Source: Deloitte analysis

What do customers want?

Convenience, service, value

As banks and building societies have introduced direct banking channels over the last 20 to 30 years, the need for customers to visit a branch in person has lessened. Over time, the use of these direct channels has overtaken the branch, with the majority of retail banking transactions now being processed via call centres, the Internet and mobile devices. Some commentators have even proposed that the rise of digital channels will eventually render the branch redundant.[10]

As a consequence, the branches of the traditional high street banks and building societies have suffered from chronic under-investment as innovations have focused instead on online and mobile banking. And thousands of branches across the country have been closed in the last decade as footfall has plummeted.

One side-effect of this systematic shrinkage in the physical network is a reduction in brand awareness. Previous studies have shown that customers struggle to differentiate between the traditional retail banking institutions in the UK.[11]

Yet this new research shows that customers vary in their needs and expectations from one micro-market to another across the country or even across the branch network of a single bank or building society. And, despite the growing influence of direct banking, the branch remains a key point of contact with customers.[12,13] Indeed, primary research conducted by Deloitte in November 2013 indicates that nearly three-quarters of consumers still usually go to the high street, shopping centres or retail parks to access banking and financial services, with more than two-thirds of consumers saying they will continue to do so in the next six months.[14]

Understanding these variations and their potential impact upon branches should provide an opportunity for retail banking institutions to position their footprint, formats and products more effectively to create greater differentiation, increase propensity to purchase and reconnect with customers who cannot get everything they need from digital channels.

For example, Metro Bank is Britain's first new high street bank in over 100 years. Their branches are referred to as 'stores', which they are using to "reinvent the rules of retail banking".[15] Metro Bank stores are located primarily in Super Conurbations with an expanding network in Commuter Zones. Deloitte's analysis shows that customers in these locations are likely to be younger than average and also Internet and mobile savvy. Nevertheless, their relative wealth and early life-stage suggest that they are more likely to want a mix of competitively priced products, convenience and face-to-face services than a largely online bank that offers very little physical interaction.

In Super Conurbations, Commuter Zones and Traditional Urban Centres, the combination of a predominantly young customer base – particularly in the 16-to-24 age-range – creates an opportunity for branches to not only enhance service differentiation but also increase sales of products, which customers are still keen to arrange in branch rather than online.

The relationship between location segment and customer needs can help retail banking institutions achieve greater differentiation and cost efficiencies around the three dimensions of convenience, service and value. Based on the primary characteristics of each micro-market segment, it is possible to hypothesise the likely implications for 'local' customer needs, as illustrated in Figure 12.

Making practical changes to provide a superior first experience around anchor products may deliver a range of benefits, including higher footfall, improved customer satisfaction and an increase in long-term customer loyalty. Moreover, marrying the right products to the right micro-market may also improve a customer's propensity to purchase other products in the branch. For instance, previous Deloitte research suggests that those customers with cash Individual Savings Accounts (ISAs) own on average 5.8 products and those with mortgages own 5.9, while those with current accounts own 4.2.[16]

72%

of consumers said that they still usually go to the high street or shopping centres to access banking and financial services

Figure 12. What do branch customers want?

	Convenience	Service	Value
Super Conurbations	• Clusters of branches, or individual branches with a large, contemporary retail format, to accommodate high footfall at peak times and in locations close to worker centres and on high streets	• Balance between efficient self-service facilities for city workers and dedicated informal space for experienced members of staff to guide customers through purchase of products	• Competitively priced products, but not necessarily the cheapest
Commuter Zones	• Branches with extended opening hours, including weekends, located near transport hubs	• Personalised, high-quality concierge service and formats coupled with rapid support for everyday transactions to reduce queues at critical times	• Competitively priced products, although convenience and service are more likely to be important
Retirement Areas	• Branches that open later in the day and are in the vicinity of other local shops and amenities	• Friendly, hands-on support for self-service channels and straightforward over-the-counter transactions	• Convenience and service are more likely to be important
Booming Towns and Villages	• Branches close to tourist 'hot spots', where hotels and restaurants are clustered	• Balance between self-service facilities and dedicated resources to guide customers through purchase of anchor products	• Local incentives and product offers for new customers
Declining Rural Communities	• Branches or branch services co-located with other retailers	• Streamlined formats focused on efficient self-service and remote support for product guidance where necessary	• Affordable products, as well as convenience
Struggling Blue-Collar Districts	• Branches in close proximity to or co-located with other retailers	• Streamlined formats focused on efficient self-service and remote support for everyday transactions	• Affordable products, as well as convenience
Traditional Urban Centres	• Branches with a contemporary retail format and extended opening hours, located within walking distance of business centres, shops, colleges and universities	• Dedicated customer service to provide product guidance coupled with streamlined formats focused on efficient self-service	• Local incentives and product offers for new customers, especially students and the newly employed

Source: Deloitte analysis

Streamlining service provision

Mismatches between current branch locations, formats and customer needs can point towards potential network inefficiencies and a higher cost-to-serve. Continuing to offer primacy to costly face-to-face services in locations such as Retirement Areas, Declining Rural Communities and Struggling Blue-Collar Districts will only ratchet up the pressure on cost-to-income ratios for branches in these segments.

For example, discussing his bank's intention to close more of its UK branches, Ashok Vaswani, the head of retail and business banking at Barclays, recently said, "I'm a firm believer that branches will survive but the format – where they are located and what happens in them – will change".[17]

Technology will clearly play a role in helping to streamline internal processes and service provision – and thus reduce costs. For example, video-conferencing facilities may significantly reduce the need for branches in some micro-markets to maintain a cadre of product specialists while simultaneously allowing customers to interact with appropriately trained people in call centres or other branches where members of staff have greater capacity. And adopting a common technology platform and look-and-feel across in-branch and digital channels will make transactions more intuitive and help customers to self-serve while potentially reducing costs.

Balance across segments

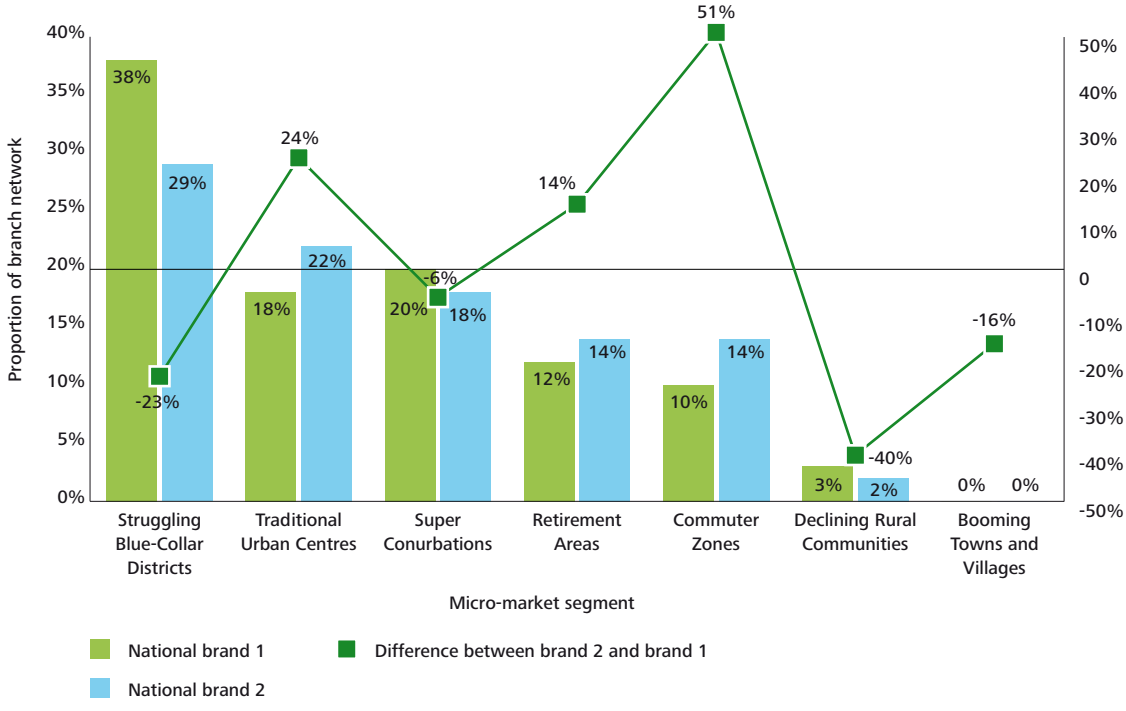
Decisions about new openings, format changes or closures can be further informed by looking at how many branches of a network are located in each of the seven segments. Geographic spread needs to be balanced against micro-market variation to maintain the ideal efficiency of the branch network and reduce the cost of implementing many different formats. This is particularly relevant for regional brands whose heartlands may be a diverse mix of micro-markets.

A study of the composition of one brand's network against the national average can reveal those segments in which the institution is under- or over-represented. Equally, comparisons between two or more brands can provide useful insights into competing location strategies or propositions.

For example, Figure 13 shows a comparison between two national brands, both of which have over 600 branches. The chart shows, for instance, that Brand 2 has 50 per cent more of its network in Commuter Zones than Brand 1 but 23 per cent less in Struggling Blue-Collar Districts. All other factors being equal, these differences suggest that the right decisions to optimise Brand 2's network – focusing on banking convenience and the quality of face-to-face services in branch – are not necessarily the right decisions for Brand 1's network – where efficient services as well as affordable products are likely to be more important.

For Brand 1, the pertinent questions are around the size of the current footprint in relation to footfall, and there is potentially a case to be made for branch rationalisation. However, the opposite may hold true for Brand 2, where the challenge appears to be twofold: how to bring mass-market banking to areas that are currently not served by its branches, and how to maximise revenue in existing branches by tapping into the latent demand for products in primary catchments.

Figure 13. Comparison of network profiles for two national brands



Source: Deloitte analysis

London: A tale of many cities

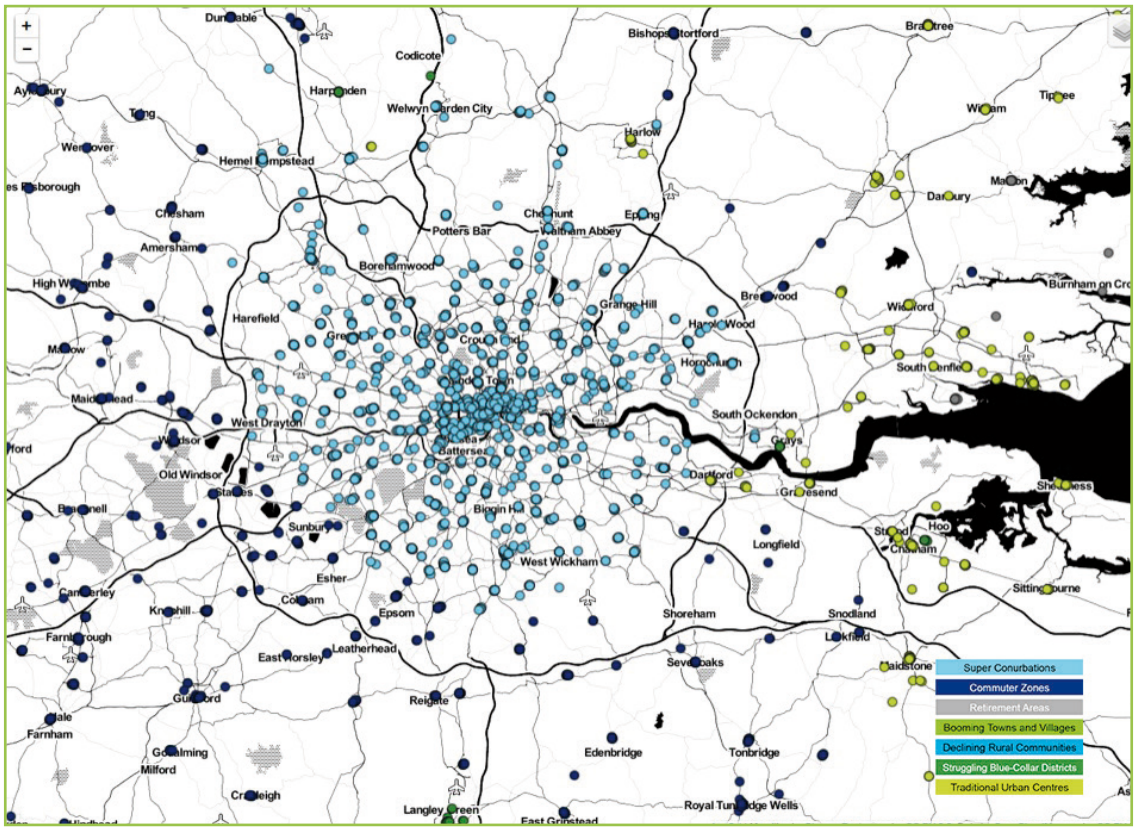
A number of different market segments may be present at the scale of large cities and their surrounding suburbs. For example, Figure 14 shows the locations of bank and building society branches in Greater London and the region surrounding the city.

Although the majority of branches here are classified as belonging to Super Conurbations, branches to the south, west and south-west, including the towns of High Wycombe, Slough, Reading and Guildford, are in Commuter Zones. Many of the towns to the east of London, such as Dartford, Basildon and Chelmsford are Traditional Urban Centres, with some coastal areas of Essex classified as Retirement Areas. Finally, branches in towns such as Crawley and Welwyn are in Struggling Blue-Collar Districts.

Figure 14 reveals yet another layer of complexity for banks and building societies. At the scale of a bustling metropolis, branches can no longer be considered in isolation, removed from demographic or economic changes occurring elsewhere in the network. Instead, the branches collectively form a more intricate ecosystem, which itself needs to be optimised for footprint and format according to the drivers of convenience, service and value.

A practical consequence of this clustering is that branches which serve the same market segment could share the load between them. This is particularly valuable in segments where footfall is expected to be high, including Super Conurbations, Struggling Blue-Collar Districts and Traditional Urban Centres.

Figure 14. Bank and building society locations in Greater London and its environs



Source: Leaflet, OpenStreetMap contributors, map tiles by Stamen Design, Deloitte analysis

For example, branches could provide a common set of services, with customers seeking to purchase products being given appointments in branches according to where spare capacity exists. Alternatively, the branches could specialise in particular products, with customers being served in the particular branch that best meets their requirements.

In reality, the level of flexibility may be constrained by more practical matters, such as branches with varying building layouts or terrain features that separate them. Thus a hybrid approach, between the two extremes, may be closer to the optimum solution.

Greater London's branch network is more complex still. Even though branch catchments have been classified as belonging to only one of the seven market segments, there are some noticeable differences between them. Further insights can be gained by sub-dividing Super Conurbations into distinct micro-market segments, as illustrated in Figure 15.

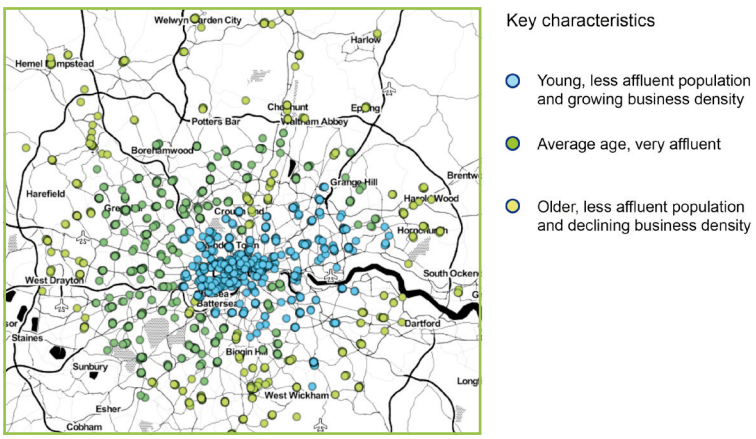
Branches to the suburbs west of London, for example in Richmond and Hammersmith, serve a very affluent residential population of near-average age, whereas the customers of branches in the southern and northern outskirts, which include Croydon and Watford, typically have relatively lower incomes and an older population. In central London, the percentage of 16-to-24 year-olds is higher than in the outskirts, but incomes are lower still.

However, the principal differences between London's micro-market sub-segments appear to be defined by a combination of age, personal wealth and business demography, which, in turn, should have a significant influence on branch formats in various locations throughout the city. For example, flagship city centre branches are seeking to serve a more transient but very substantial daytime worker population as well as the transactional needs of local businesses. In the suburbs to the south-west, branches are likely to be dealing with more mature and affluent residents. Changes made to the format of a branch in any one of these sub-segments may have a knock-on effect on other branches nearby even if those branches serve different market sub-segments.

This cascading effect could be either positive or negative. For instance, cutting back on face-to-face services in the south-west may actually increase footfall, especially of new product seekers, to the city centre. But branches there may struggle to meet the demand.

Where journey times between branches of different segments or sub-segments are less reasonable, though, careful thought needs to be given to how branches can provide an adequate range of banking services and products to meet all the possible customer needs in an area. This is the point at which additional data, including data on operating costs, product sales, transaction volumes and customers, as well as data from other internal sources, should be used to fully optimise branch networks.

Figure 15. Example showing market sub-division in Greater London



Source: Leaflet, OpenStreetMap contributors, map tiles by Stamen Design, Deloitte analysis

Towards network optimisation

In his 1988 Precision Marketing article, "The Need to Rethink Analysis", John Whitehead coined the phrase "micro-marketing".[18] His concept acknowledged that markets can no longer be considered homogenous. Twenty-five years later, the markets in which bank and building society branches operate are more diverse and dynamic than ever. So much so that decision-makers who assume that the battle for branches has already been lost to direct channels are in for a surprise.

Although half of regular Internet users in Britain now bank online, and the number of people expected to use mobile devices for banking activities is expected to double by 2016, decisions about the future of branches can only be taken after considering what customers want, in terms of convenience, service and value.[19,20] This can vary considerably from one location to another. And while the size of the country's total branch footprint may indeed shrink as further digital innovations are introduced, new entrants are attempting to show that branch banking can make a comeback where micro-markets work in their favour.

This research has demonstrated that a wide range of demographic, business and economic factors – both static and dynamic – are needed to understand micro-markets. But despite this inherent complexity, current branches in England and Wales fall into just seven key segments. In each segment, the characteristics of the micro-markets are broadly similar; across segments, they are very distinct.

In some segments, especially those with a younger demographic, the micro-market characteristics suggest that in-person rather than direct channels should be the basis for improving customer experience and retention, and more effective cross-selling. In other, older or less affluent segments, where the branch tradition has typically always been strong, a focus on greater transactional efficiency should help to reduce costs as more customers switch to direct channels.

To drive lower cost-to-income ratios and maximise opportunities for revenue growth, this kind of counter-intuitive thinking is required. Successful banks and building societies are likely to be those that create the right balance of convenience, service and value across their network, incorporating not only the most appropriate changes to format and service for individual branches, but also discovering the optimum branch proposition across regional areas.

It is no longer sufficient to say that banks and building societies need to mobilise a multi-channel or even an omni-channel strategy. Getting the mix of telephony, Internet, mobile, ATM and branches right remains important but Deloitte's research suggests that location as well as channel mix will drive success. It is also a virtuous relationship: understanding micro-markets will help to get the branch format right; getting the branch format right will help to get the network right; and the branch remains crucial to creating service differentiation and for building new, long-term customer relationships.

Decision-makers who assume that the battle for branches has already been lost to direct channels are in for a surprise.

Drawing such crisp battle lines around digital and physical may have spurred tremendous technological innovation, but it has also left behind a legacy of underperforming branch networks.

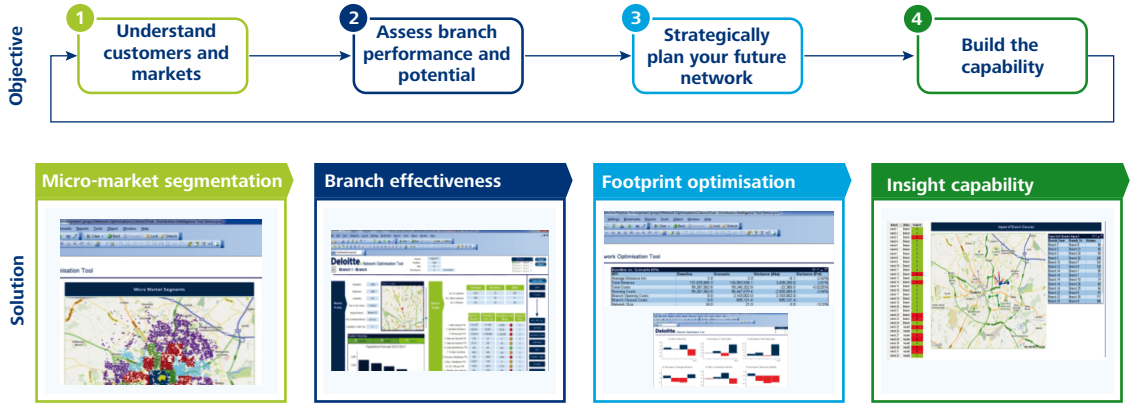
While the branch may never become fully extinct in any of the possible future banking scenarios, if multi-channel strategies do not take into account the rich micro-market context, such investments may do more harm than good. They may create massive imbalances across the network, stifling revenues and raising some branch cost-to-income ratios to unsustainable levels.

As more data becomes available from public, commercial and internal sources, banks and building societies can harness advanced analytics to optimise their networks in four simple steps, as illustrated in Figure 16.

In practice, no single solution will materialise to help all banks and building societies optimise their branch strategy. Each financial institution should tailor its own network to meet their brand's particular objectives and the dynamics and trends in their target markets.

Although many banks and building societies are currently rethinking their branch strategies, arguably few have taken steps to understand the complex relationship between what customers want and where they are located. Only those that build their branch proposition based on the most appropriate balance between 'bricks and clicks' are likely to succeed.

Figure 16. Four steps to network optimisation



Source: Deloitte

Appendix: Methodology

Calculation of catchment areas

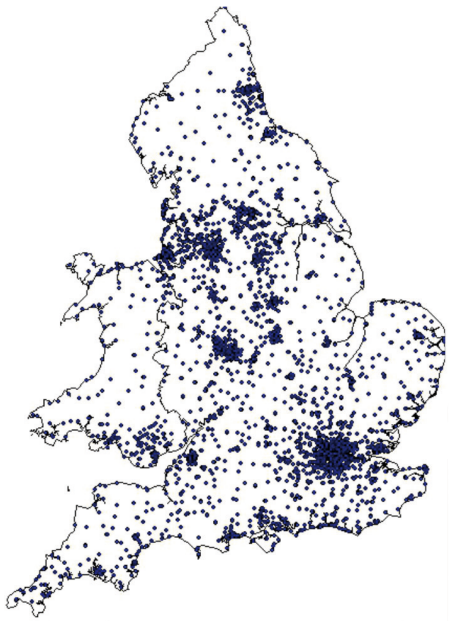
To get to grips with local market dynamics, one first has to understand the complex relationship between branch footprint and customer footfall. This is because an increase in the number of branches in a network does not necessarily translate into a proportional increase in the population coverage, and vice versa. Coverage depends on where the branches are and how big their catchment area is.

Figure 17 shows the locations of the 10,433 bank and building society locations considered in this research.

A catchment area is the population from which a branch draws its customers. For the purposes of this research, the 'pull' of a catchment area depends upon:

- the number of other branches, including branches of the same bank or building society in close proximity
- the number and quality of other shops and supermarkets in close proximity
- the amount of time it takes for the population from a given area to travel to the branch, with people living farther away less likely to travel.

Figure 17. Bank and building society locations



Source: Local Data Company, Deloitte analysis

Catchment areas are calculated by first clustering neighbouring branches and other shopping centres into 'retail centres'.

By including shopping centres in the analysis, a much better appreciation of population flows can be developed than if bank or building society branch locations were considered in isolation. The impact of competition and the co-location of branches with other retailers can also be captured. However, although many of the catchments in towns and cities will include tens or hundreds of bank or building society branches and shops, rural areas will be sparsely occupied – and some catchments will include only the 'last bank in the community'.

Gravity modelling

After clustering, a probabilistic gravity model is used to build a set of overlapping catchments.[15] The gravity model determines how likely it is that people living in the surrounding area will travel to one particular retail centre rather than any other based on its attractiveness – the presence of bank branches, leading retailers and other brands trading in local high streets and shopping centres – and the amount of time taken to drive from where they live to the centre.

In the absence of more detailed population flow data – such as anonymised mobile phone location data – it is reasonable to assume that people seeking services will travel to the most attractive centre within a reasonable drive time.

Segmentation

Alongside population flows, our gravity model is also used to calculate 56 demographic and economic statistics for the micro-markets surrounding each of the approximately 2,300 catchments.

Important variables in the analysis include the size of the local population and their age, employment status, income and expenditure. We have also included data on the number of people who bank online, the nature and number of local businesses, particularly retailers and small businesses, and other economic factors, such as local house prices and worker productivity.

And, key to this research, our approach includes data describing the amount of change forecast to occur in each of our static variables over the next five years.

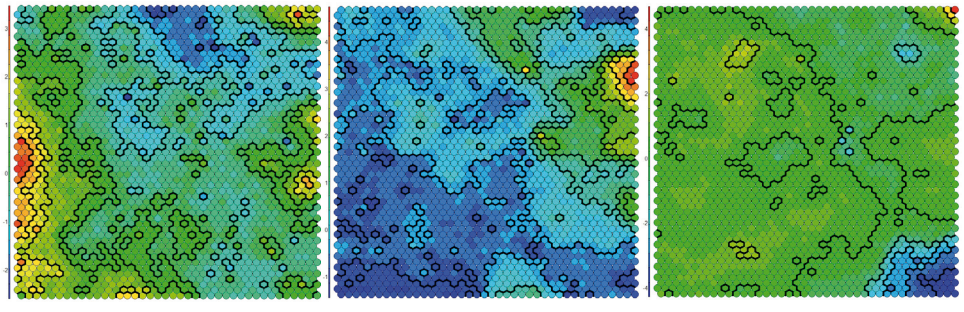
The catchment statistics are then clustered using a technique known as Self-Organising Maps (SOMs). SOMs try to position catchments that are similar in highly dimensional space into a configuration where they are close to each other in a lower-dimensional 'map'.

An example of the outputs of an exploratory SOM analysis is shown in Figure 18. Each cell in these two-dimensional images represents the micro-market of a single catchment. The position of the micro-market in each map is the same but it is not related to its real-world location. Rather, it has been optimally positioned by the SOM algorithm so that it is surrounded by other catchments whose characteristics across the 56 dimensions are most similar.

Finally, a hierarchical clustering technique is used on the output of the SOM to determine how many segments are needed to describe adequately the different characteristics of all catchments in England and Wales.

Figure 18. Two-dimensional 'heatmaps' of the output of the Self-Organising Map for three catchment statistics

From left to right: Mean age, disposable income and percentage change in population of people aged 65 and above



Source: Deloitte analysis

Notes

1. "Bring back the branch", Deloitte & Touche, September 2002. See also: http://www.finextra.com/finextra-downloads/featuredocs/MS_RetailBanking_summary.pdf

2. "Winning with branches – Six disciplines for branch transformation", Deloitte & Touche, 2007. See also: http://www.deloitte.com/assets/dcom-unitedkingdom/local%20assets/documents/uk_fs_sixdisciplinestobranchbanking.pdf

3. "The Deloitte Consumer Review – Reinventing the role of the high street", Deloitte LLP, November 2013. See also: http://www.deloitte.com/assets/Dcom-UnitedKingdom/Local%20Assets/Documents/Industries/Consumer%20Business/uk-cb-consumer-review-edition-6.pdf

4. "Branch Network Reduction: 2013 Report", Campaign for Community Banking Services, August 2013. See also: http://www.communitybanking.org.uk/report_reduction_2013.htm

5. Ibid.

6. "Bridging the advice gap: Delivering investment products in a post-RDR world", Deloitte LLP, 2012. See also: http://www.deloitte.com/assets/Dcom-UnitedKingdom/Local%20Assets/Documents/Industries/Financial%20Services/uk-fs-bridging-the-advice-gap.pdf

7. Data provided by the Local Data Company, September 2012.

8. The gravity model used in this research is an extension of that referred to in "A Probabilistic Analysis of Shopping Center Trade Areas", Huff, D, Land Economics, 39, 81-90, 1963.

9. The Grimsey Review, "An Alternative Future for the High Street", September 2013. See also: http://www.vanishinghighstreet.com/wp-content/uploads/2013/09/GrimseyReview04.092.pdf

10. "Do bank branches just need a makeover?", BBC News, April 2013. See also: http://www.bbc.co.uk/news/business-22152611

11. "Winning with branches – Six disciplines for branch transformation", Deloitte & Touche, 2007. See also: http://www.deloitte.com/assets/dcom-unitedkingdom/local%20assets/documents/uk_fs_sixdisciplinestobranchbanking.pdf

12. "There is a future for the bank branches", a joint report by Deloitte Belgium and the Vlerick Leuven Gent Management School, 2009. See also: http://www.deloitte.com/assets/Dcom-Belgium/Local%20Assets/Documents/TheFutureOfBranches_Report_Feb2009.pdf

13. "Innovation in Retail Banking 2012: Growth of Channel Innovation", EFMA, 4th Annual Edition, September 2012.

14. "The Deloitte Consumer Review – Reinventing the role of the high street", Deloitte LLP, November 2013. See also: http://www.deloitte.com/assets/Dcom-UnitedKingdom/Local%20Assets/Documents/Industries/Consumer%20Business/uk-cb-consumer-review-edition-6.pdf

15. See https://www.metrobankonline.co.uk/Discover-Metro-Bank/About-Us/

16. "Winning with branches – Six disciplines for branch transformation", Deloitte & Touche, 2007. See also: http://www.deloitte.com/assets/dcom-unitedkingdom/local%20assets/documents/uk_fs_sixdisciplinestobranchbanking.pdf

17. "Barclays warns of more UK branch closures", Sharlene Goff, Financial Times, 17 November 2013. See also: http://www.ft.com/cms/s/0/e90e3854-4fa6-11e3-b06e-00144feabdc0.html#axzz2lkosYdsw

18. "The Need to Rethink Analysis", Whitehead, J., Precision Marketing, November 1988.

19. "Internet Access – Households and Individuals 2013", the Office for National Statistics, August 2013.

20. "EFMA Mobile Banking survey", 2011.

Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675 and its registered office at 2 New Street Square, London EC4A 3BZ, United Kingdom. Tel: +44 (0) 20 7936 3000 Fax: +44 (0) 20 7583 1198.

Designed and produced by The Creative Studio at Deloitte, London. 32274A