JONES LANG LASALLE®

Real value in a changing world

Global Retail Banking

Key trends and implications for retail banking real estate

Retail *2020*

Developed World
Network
Call Centres
Good Ethics
Branch focus
Developing World Frontier Markets
Retail Banking
Technology
Easy Finance
Global Banking
M-banking
Game Changer

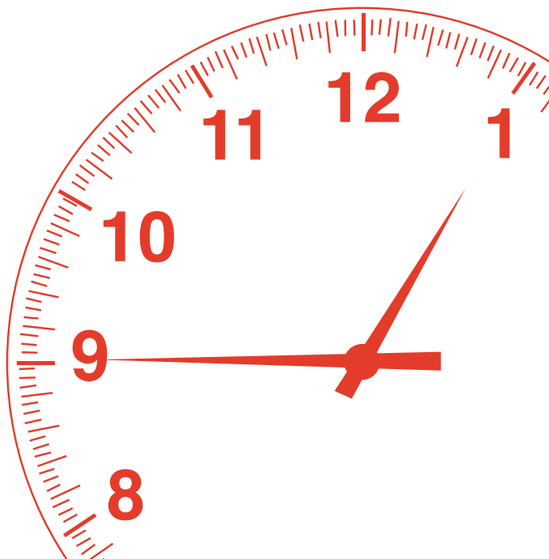
Predict or get left behind

The new normal is economic uncertainty and marketplace volatility. Weakening growth in the developed world, allied with a lack of political leadership is unnerving markets and business leaders alike. As this report goes to print, the eurozone crisis rumbles on (or even worsens). Meanwhile, the political stand-off in America is adding to the sense that leading authorities will make a fatal miscalculation. At the heart of all of this, still, are the banks. Despite the stress tests, there are too many unknowns for any complacency. How many toxic assets still sit on bank balance sheets? How far will low economic growth or any rises to interest rates, cripple the banks' loan books? What are the counterparty risks? How quickly could sovereign insolvency and bank illiquidity lead to a meltdown of confidence, a drying up of the interbank market and a second credit crunch? To what extent will regulation force restructuring in the banking industry? Which bank is the next to fail or to need government support?

Meanwhile, the picture in the developing nations and frontier markets could not look more different. By and large we are looking at an increasingly decoupled world where Asia (and other emerging markets like Brazil) are reaching a self-sustaining cycle with far less dependency on the USA and Europe. On-going trade surpluses are raising domestic demand little by little. Economic growth has recovered quicker and to much higher levels than in the developed world. Meanwhile, banks in China, India and beyond, cleansed a lot of their bad debts in the 1990s and capital ratios are in better financial shape than in the West. Despite occasional nervousness about bad loans (e.g. in Chinese local government), and a marginal weakening in economic outlook, the still strong GDP expansion means that, overall, banks in developing countries are looking forward to a decade of profitable growth.

With such macro-economic instability (and divergence), geo-political and balance sheet uncertainty, who'd be a forecaster? And yet it is vital to get our hands around the future. Yes, the exact future is unknowable, but it is possible to anticipate plausible outcomes which can then inform decision-making today. Better to predict, assess probabilities and prepare than sit back and become the victim of future changes.

It is in this spirit that Jones Lang LaSalle has written this report on Retail Banking, 2020. Using desk research, expert interviews and industry round tables across three Continents, we have taken a 360° tour of the horizon. We have looked at political, economic, technological and socio-cultural trends. Bringing this together, we have then analysed the knowns, taken a view on the unknowns and derived a plausible vision of where retail banking is going internationally, and what the knock-on effects will be for real estate markets.



Executive Summary

1. Economic and Political Context

- The after-shocks of the Great Recession will continue to be felt over the decade
- Low, hesitant growth in developed countries will herald marketplace consolidation as well as provide encouragement for overseas expansion
- The developing world is increasingly decoupled and GDP growth will be much stronger here
- Politically, the next decade will be one of interference and regulation; in this respect, the political situation in the developed and developing world will become more aligned
- The tide is moving against big banks: 'too big to fail' has become 'too big to bail'
- This will give rise to a climate of uncertainty and conformity but potentially also greater flexibility and retail bank autonomy; nimble banks will profit
- The trap for banks will be to become obsessed with the regulatory situation (compliance and risk mitigation) and lose their consumer-facing - and technological – focus

2. Key Drivers of Change

Power to the people
- Banks can no longer rely on customer loyalty nor inertia: their customer base is increasingly mobile
- Overall, people are increasingly savvy regarding their finances: they will demand more from their bank – become more prudent and untrusting
- Banks are losing their 'one-stop-shop' status and more people will build a portfolio of financial service providers
- Three key consumer trends to watch for are: Easy Finance, Good Ethics, Independence
- All told, the above dynamics will accelerate the move to online banking, place a greater emphasis on service in branch and catalyse a drive to target the wealthier segments with a differentiated offer

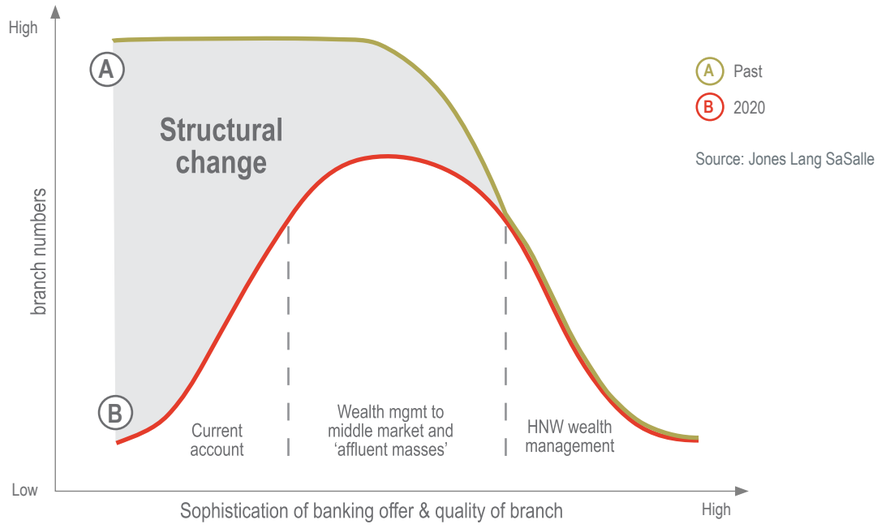
Technology – the game changer
- The internet will be the disruptive force to the banking sector over the decade
- Customers' love of online banking means that it will become the key touchpoint
- Banks have 'transposed' internet banking onto their business but will need more seamless integration going forwards
- As in retail, technology, and M-banking specifically, is the game changer, particularly in the developing world
- The impacts of technology will be felt in: channel integration, smaller branch networks; non-bank led disintermediation; the configuration and targeting of international roll-out programs
- The move to a new platform is opening the way to non-bank competition who have increasing advantages over incumbents – no legacy systems or branch networks

Image is everything
- All banks will be working to claw back lost trust to ensure that, by decade's end, their tarnished image will have turned positive once more
- They will up the ante in innovation – for different target customers and within the branch network
- Promising areas for innovation include: Shariah finance, delivering 'social value', and managing intelligence

3. Implications for Real Estate

Branch numbers
- The age of the big branch legacy network in developed world countries is drawing to a close
- The twin drivers of technological advancements and higher levels of financial sophistication amongst consumers will fundamentally alter the size and structure of bank networks
- America and Europe in particular are over-banked and are witness to a rationalisation of branch numbers and a reduction in branch footprints. As many as 50% of branches in networks may be declared obsolete in their current form in the developed world by the decade's end.

Structural change in retail bank branch networks



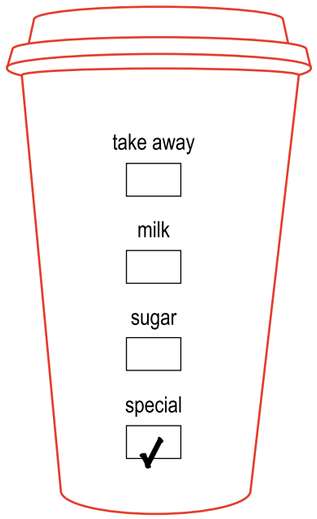
- However, banks have too much invested in their branch networks to engage upon a radical disposal programme and a mixed 'bricks and clicks' strategy will define the decade ahead
- In the majority of instances, lease expiries will be the catalyst for change
- Conversely, some branch expansion will happen, in certain markets of the developed world, from new indigenous entrants to the banking world
- However, the majority of bank expansion will happen in developing countries, where there is significant room for banking growth. India in particular is hugely under-banked, and the market is now ripe for development
- Bank branch saturation will be avoided in most developing world markets, as new technologies and geographical constraints make large branch networks unneccessary
- We will see continued flows of funds from the developed world to the developing world as established banks seek profitable opportunities: progress will be cautious due to high entry barriers
- There will also be heavy investment by indigenous banks in local markets in developing countries where they have inherent advantages

Branch networks

- Around the globe, we will see continued experimentation with formats and locations - getting the right mix of mobile, direct and location-based channels will be crucial.
- Branch focus will be on service, sales and relationship building as transactions are pushed online or through call centres
- Wealth management services to the affluent masses will become a key battleground
- Expect the hub and spoke model to gain prominence, whereby premium flagship branches in big cities cater for the more sophisticated products and services, and smaller satellite branches give access to basic banking services
- In much of the developing world, competition for prime retail space will be a fact of life and many banks will lose out to retail brands and more aggressive competitors
- In addition to branch real estate strategy, in both the developed and developing world, future location strategies for datacentres will loom large, as digital technologies dramatically increase secure data storage requirements

Banking environments

- Banks' key challenge is to make branches relevant for customers in the internet age and therefore be an attractive tenant for landlords
- Banks are becoming more like coffee shops – will we see a move towards more formal JV tie-ups, or even the Bank of Starbucks?
- The quality of the banking environment, therefore, will be improved – through service initiatives, technology initiatives, redesign, innovation and a focus on ecology; the move towards the 'retail model' will continue its insatiable progress



Branch focus will be on service, sales and relationship building as transactions are pushed online or through call centres

Economic and Political Context

Angst vs optimism: a tale of two worlds

The future of retail banking will be a story of two worlds - developed and developing

DEVELOPED WORLD

For the developed world, the big question is, will the policy measures taken since the Great Recession stabilise global financial and banking systems. While the worst danger appears to be over, there remains downside potential over the next 3-5 years, why?

Deleveraging: Post-crash consumer deleveraging has a distance to run. McKinsey's Global Institute research showed that America is only one third through its adjustment and Britain may take to the end of the decade to return to pre-crash levels.

Sovereign debt exposure: European banks' exposure to the sovereign debts of the fringe Eurozone economies presents a new risk to the global financial system. Recent ECB emergency loans have alleviated the problem, but the underlying capital position is weak.

Social mood: Meanwhile, the social mood is fragile and much discontent is focussed on banking, so further reactive policy and regulation may be in prospect.

In the short-term, banks will continue reducing headcount and restructuring balance sheets.

Once the recovery is established, a more strategic response will be necessary along the following lines:

Cautious lending: There will inevitably be greater caution about extending new credit, reinforced by tighter regulation and supervision.

Selling off surplus assets: This process will continue and include changes to the branch network as banks respond to changing technology and behaviour, and further disposal of peripheral businesses and assets, including property.

Consolidation: It is likely that by the end of the decade we will have fewer, but larger Europe-wide banks, as smaller institutions cannot compete in the 'new world'.

Re-orientation of growth: In the developing world, a growing middle-class will bring vast savings to be re-cycled globally and new demand for finance in the developed world.

DEVELOPING WORLD AND FRONTIER MARKETS

If we look at finance in the developing world, where growth prospects are likely to be notably higher, there are important differences:

Healthier growth prospects: Emerging markets bounced back much more strongly after 2008 and domestic demand and savings remain healthy. Growth rates between 5-10% are forecast, far above the rates in the developed world.

Greater resilience to global shocks: The legacy of the global financial crisis will be less of a burden. Many emerging markets have tightly controlled financial sectors and low levels of indebtedness, which has reinforced their ability to withstand recent shocks.

This is not to say the developing world's financial systems are immune, of course, as banking has often been central to past crises there. The difference is how fast these relatively immature and un-globalised sectors have recovered, when compared with the grim experience in the developed world.

The tide is moving against big banks; 'too big to fail' has become 'too big to bail'

Political context and regulation

Financial markets in the developed world have seen many pendulum shifts over the last century. After the 1980s, liberalisation and self-regulation became the priority. Today, the pendulum is swinging the other way.

Looking ahead, the next ten years are going to witness movement towards intervention and away from discretion in the developed world. Politicians, central bankers and regulators will play a more significant role in the future of banks over the next decade – both as rule makers and as stakeholders in many countries (albeit a certain amount of caution is needed, so as not to overburden banks with regulation; witness HSBC's recent warning shot). Extra public funds may be required to bolster this process and prevent a repeat of the credit crisis.

The tide is moving against big banks; 'too big to fail' has become 'too big to bail'. The future will see an enforced separation of risky investment activities from retail banking, with the Vickers Report in the UK leading the way.

And the possible consequences for retail banks over the decade?

Uncertainty: Given the politicisation of banking, the environment will be harder to predict with absolute certainty and so operating conditions will be more challenging.

Conformity: Banks will face a much heavier compliance burden than in the past. They will need to consider the impact on customers and not use this as an excuse to stifle innovation.

Autonomy: Retail banking will be valued as a business in its own right and not as a poor relation to investment banking.

Flexibility: Agility will become key, as factors such as effective property management, and flexible/responsive working practices will be vital in securing competitive advantage.

Consumers will be demanding more from banks at the very time when they are most distracted. Nevertheless, these challenges will give the very best operators a chance to shine.

Drivers of Change

1. Power to the People

An end to inertia: savvy consumers will change banks more frequently

DEVELOPED WORLD

Consumers becoming increasingly financially aware...

It wasn't too long ago when people in the developed world would get dressed up to see their branch manager and sit trembling waiting for their turn. How quickly things have changed! On one side, banks themselves, progressively, have divorced themselves from their local communities. On the other, people have become more knowledgeable and clued up about their lives and their financial decisions. Of course, the fast, accessible internet is proving to be the great leveller of information and liberator of 'consumer' power.

This empowerment will result in more people switching between current bank accounts. Back in the 1980s, the anecdotal figure of those changing main bank over their lifetimes was quoted at 8% for the UK. But in surprising figures from JD Power, 8.7% of American customers switched bank in just one year (2010-2011). In 2009-2010 this was only 7.7%. And banks like Santander actively encourage switching by incentivising non-customers to transfer their account. Clearly consumer empowerment will translate into less inertia and lower loyalty. We have already seen this trend in other financal services such as insurance.

Meanwhile, past inertia has been encouraged by the view that 'all banks are the same'. Over the next decade we will see retail banks rushing to introduce new charges on their retail customers – eg. for the use of debit cards; on current accounts and so on. Whilst herd instincts mean that 'when one bank goes, they all go', we will inevitably see different pricing structures between banks and certain sharp eyed customers will read the small print and choose their bank accordingly. Again, this means less inertia going forwards.

People power will also mean a refusal by customers to see their main bank as a one-stop shop for all financial services. In the future, customers will, increasingly, resist pressure for on-selling and cross-selling. They will be helped in this direction by a host of new online financial service offers, each one disintermediating the banks' full line offer. Non-bank companies like America's National Life Group offer an increasingly sophisticated range of financial services products. Meanwhile, price and service comparison sites will only accelerate the customer's move to a portfolio of financial service providers. As so often, disintermediation will happen due to a thousand small bites rather than one big gulp.

People power will continue to demand more honesty, improved quality, transparency

Clearly consumer empowerment will translate into less inertia and lower loyalty

....and therefore more demanding.

Increasing financial awareness may bring with it a new prudence, giving rise to three specific consumer trends over the next ten years:

1. Easy Finance: customers want speed and they want ease of use – banks will have to deliver and improve their hygiene standard over the decade. For example, ING Direct USA is aiming to reduce the pain of using an 800 number to contact a call centre representative: it is not intuitive, straightforward nor easy to use.

2. Good Ethics: According to Edelman's Barometer, trust in banks has fallen off a cliff. Global figures show 56% trusted banks in 2008, falling to just 40% by 2012. Unsurprisingly, people are looking for a higher moral code in their leaders and institutions. Bashing banks has been commonplace over the last 5 years and will continue across the decade, reaching a peak in the West, as the economic slide continues towards the middle of the decade. People power will continue to demand more honesty, improved quality, transparency, a clear sense that banks are on their side. Until banks have restored trust and confidence, they can expect to be treated suspiciously and see migration to newcomer competition with unspoilt images.

3. Independence: people increasingly want to own their finances and feel in control. This means that they will judge banks increasingly on their: impartiality, quality of information, straightforward dealings and service culture. Independence is all about having an 'adult-to-adult' relationship with a bank – and throwing off that suit and tie.

Given these trends, what are some of the implications for banking?

1. A continuing drift towards online and mobile banking: it is easier banking, gives independence and for many, has a cleaner, fresher ethical feel (it is Google's 'do no evil' philosophy writ large).

2. Wealth Management services: targeted branches will grow as customers understand that they are increasingly on their own concerning pension provision, for example. We can expect private banking to hold its own and a ramping up of the 'premium' offer of the retail banks as they rush to service the wealthier segments.

59% of adults in developing economies do not have a bank account

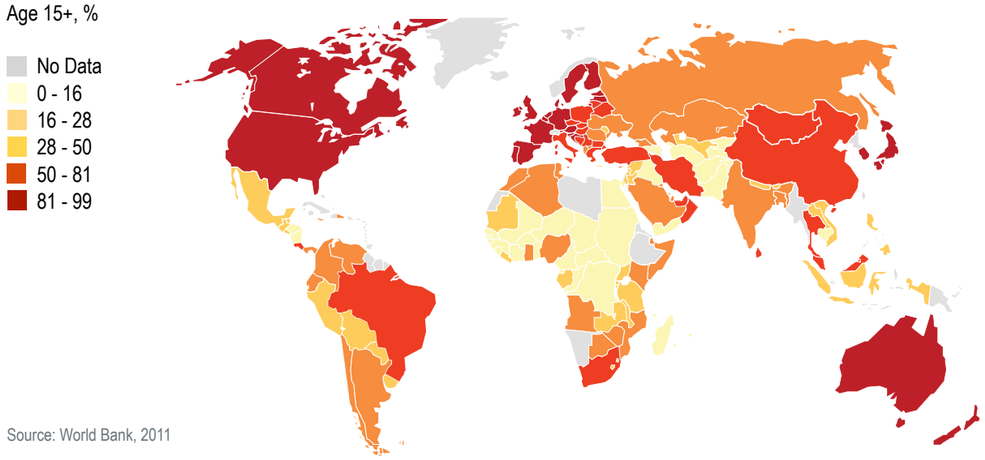
DEVELOPING WORLD AND FRONTIER MARKETS

Whilst certain elements of this 'power to the people' trend apply equally to the developing world and frontier markets, consumers are less likely to be entrenched with their legacy banks, if they have banks at all; inertia therefore represents a far less significant issue.

The Great Unbanked - approximately 2.5 billion people worldwide do not have access to banking and financial services. This is heavily skewed to the developing world; 59% of adults in developing economies do not have a bank account. In comparison, only 11% of adults in high-income economies do not have a bank account. And even within developing economies, there is a vast chasm between rich and poor; the richest 20% of adults in a country are more than three times as likely to save in a formal financial institution as the poorest 20% of adults. In all regions, with the exception of high income economies, borrowing from friends and family is the most commonly reported source of credit for current loans. 55% of borrowers in developing economies use only informal sources of credit.

The rise of M-Banking (discussed in the next section of the report) will extend the reach of financial services to a greater proportion of the world's unbanked. M-banking will also empower existing banking consumers, reduce inertia and lead to disintermediation of banking products. Mobile providers (Vodafone etc) will have a significant role to play in the future of banking in the developing world.

Global Bank Account Penetration
Age 15+, %



Source: World Bank, 2011

2. Technology – the game changer

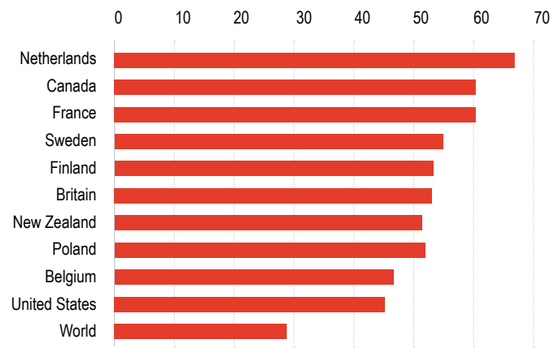
After a reasonable response to technology, banks risk totally behind

DEVELOPED WORLD

Online banking continues its inexorable rise…

Whereas some industries have been complacent and fallen victim to the power of the Web, to a degree, retail banks in the developed world have successfully gone with the flow and adapted their business to take full advantage – both in terms of cost savings and marketing. For example, most banks have successfully launched online banking for customers and blended this channel with their bricks and mortar offer. In a survey by the Bank Innovation Monitor, only 3.8% of adult Americans are unaware of online banking. On average, Americans are visiting online banking portals nearly three times a week and the Monitor found that they 'love' banking online. How many customers love their branch enough to visit three times a week?

Online banking penetration
Among total internet users, %



Source: comSorce, February 2012

Across all American banks, 55% of customers selected online as their preferred channel with only 28% choosing the branch (source: Foresee Online Banking Study, 2011). This is only set to increase across the decade. Online customers represent a significant cost saving to banks: it is reckoned to cost $0.15 to open a bank account online compared to $65 in a branch. Meanwhile, online customers have been proven to stay loyal to the channel, are 50% more likely to purchase other services, 63% more likely to recommend the bank and 63% more likely to trust their banking institution (source: Foresee 2011). Clearly, online will be the key touchpoint for banks across the decade.

Neither are banks being slow to go mobile. Recognising the potential early (there are 4 billion mobile phones in use worldwide, of which 27% are now smartphones), a full 93% of major American banks have either optimised their website for a mobile browser and/or launched a proprietary mobile app (source: Corporate Insight). The prediction that the mobile internet will overtake desktop internet usage by volume by 2014 will only serve to accelerate this movement. Meanwhile, OBR predict that the number of Americans using M-Banking will rise from around 15 million today, to 60 million by 2020.

The next decade will see further evidence of an 'online gold rush' in the banking sector from outsiders

…but further technology advances required…

Despite the undoubted success of online banking, banks need to make further technology investments, specifically in the following areas:

Developing more specific apps: banks will develop 'mobile everything' for real-time access – budgets, forecasts, payments, billing, accounts and invoices – for Apple OS and Android, smartphones and tablets.

Mobile and bill payments: particular emphasis will be given to mobile cash transfers and bill payments which are limited today compared to desktop (Chase is one bank ahead of this game).

Peer-to-peer payments: using 'bump' technologies (i.e. touching two smartphones together to pay someone $10, say). Here ING Direct and Barclays have taken a lead.

Remote Deposit Capture: i.e. depositing cheques by uploading photos of them. Chase, PNC Bank and US Bank are amongst a handful of banks currently proposing this service.

SMS banking: this will continue to be supported and even grow e.g. Bank of America will add transactional capabilities via texts.

Other technologies including: GPS marketing, biometrics (including face recognition), video-conferencing, touch screens, call centres, 3D barcodes, branch flatscreens, digital signage, account manager kiosks, branch wireless, Teller Cash Recyclers (TCR), tablet-enabled virtual desktops and radio frequency (RFID) and Near Field Communication (NFC) for e-wallet payments.

Meanwhile, all banks recognise that their legacy systems are holding back the business and many will try to accelerate migration through the use of cloud based services. They will be attracted by cloud computing's flexibility, scalability and the possibility to move costs from capital expenditure to operational expenses.

…and there are significant risks to address

The above raises certain strategic risks facing banks in the developed world concerning technology to 2020, namely:

Optimising the execution: Despite the initiatives listed above, rare is a bank which has more than half of its customers enrolled online and mobile banking uptake is much smaller still. Meanwhile, exclusively online banks (e.g. First Direct) have done well to grab market share and are generally liked and trusted, but they still serve niche markets.

On the whole, banks' websites tend to be clunky and often represent no more than a direct translation of their offline services onto the internet; insufficient thought has been given to making full use of this channel's capacities. This will be a major workstream going forwards. Mobile banking will offer similar 'translation' challenges.

Retail banks have not risen to the challenge of creating an integrated channel offer, with look and feel differing and an absence of seamless functionality and data sharing. Again this is a major task ahead since consumers see 'the single institution' and not 'the channel'. Winning banks will rise to this challenge and be rewarded through customer loyalty.

Disintermediation: Retail banks will always be protected and regulated and have the edge when it comes to moving money around securely. But around the boundaries of banking, things will change rapidly. Investments, loans and credit cards, insurance and wealth management, mortgages and pensions – these will be broken down into functional components, packaged, 'app-ed' and marketed – and much of this by non-bank competition.

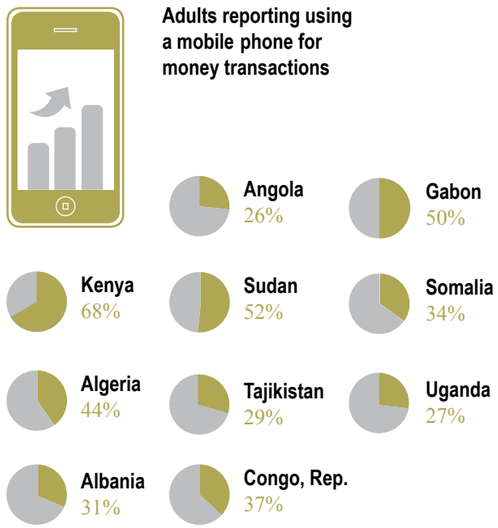
In the separate report on Retail 2020 we talked about new tech-savvy online retailers who are stealing the lunch of physical retailers. The next decade will see further evidence of an 'online gold rush' in the banking sector from outsiders. For example, PayPal is already half the size of Citigroup's global transaction services business. A disruptive player if ever there was one, PayPal reported revenue of around $4.2billion in 2011. In America, 11% of consumers have already visited personal financial management sites like Mint or Yodlee. Standard Chartered's own site, Breeze, has been highly acclaimed. Facebook's online currency will be quickly adopted by 18-30 year olds. In May 2011, Google endorsed mobile contactless payments with its Google Wallet – although mobile payments may be held back by the availability of NFC-enabled equipment.

Disintermediation is well underway, and it will happen very quickly

DEVELOPING WORLD AND FRONTIER MARKETS

M-banking to drive change…

In the developing world and frontier markets, the technology driver of change over the decade will be mobile banking. M-Banking will leapfrog both branch networks and even desktop internet, to reach very large populations in the developing world. According to INC Market Research, the gross transactional value of mobile in the Asia Pacific region will reach $29.8bn by 2013. This trend will be driven by geographical, as much as cultural, considerations. One third of adults worldwide without a bank account blame the cost of opening and maintaining an account or the banks being too far away. In Sub-Saharan Africa, where traditional banking has been hampered by transportation and other infrastructure problems, mobile banking has expanded to 16% of the market. Worldwide, those aged 15-24 are 33% less likely to have a bank account and 40% less likely to have saved formally than those aged 25-64.



Source: World Bank

Some of the biggest competitors to banks over the next ten years will be the telecoms companies

Some M-Banking operators are actively pitching to the unbanked or underbanked as the target audience for mobile services. And it's not just the banks. Here's a statistic to scare all retail bankers; in a recent survey by Amdocs published in the Banking Review, 95% of telecommunication operators in the Asia Pacific region had an active, defined strategy towards mobile payments and 84% were pursuing bill payment services. And no wonder, when you consider that phone companies have some of the most sophisticated billing systems today. It is no understatement to say, therefore, that some of the biggest competitors to banks over the next ten years will be the telecoms companies.

Vodafone's M-PESA's initiative in Kenya, Tanzania and Afghanistan for mobile remittances has caught the eye. Nokia Financial Services, Ericsson and Telecom Italia are all of the same opinion: it is the underserved banking customers who will use M-Banking first.

Over the decade then, mobile carriers will go for the high volume, low value customer first – the customer base that the banks traditionally have not wanted. By aiming at the microfinance and low profit pool, they will be seeking to attract just over 3 billion people with banking services and are confident of a profitable business model.

…but challenges to overcome

Going forwards, a number of requirements will need to be met in order for mobile banking to really take off, including: a sound regulatory environment; strong consumer protection; distribution and agent networks; market competitiveness. In an analysis by the World Economic Forum, a number of countries stood out as being in a high state of institutional and marketplace readiness for mobile. Drawing off this data, we can expect to see mobile banking make huge strides in: the Philippines, Brazil, India, Pakistan and Indonesia. Meanwhile, countries needing more of a marketplace push include: Malaysia, Columbia, Peru and Nigeria. Incidentally, in the analysis, China met market conditions but rated down the scale on institutional readiness.

3. Image Is Everything

Banks need to invent personalities.

DEVELOPED WORLD

Banks need to regain trust through innovation...

Retail banks in the developed world have a severe image problem. As we know, many people blame banks and bankers for the Great Recession and trust in banks has declined as a consequence. Research firm Marktet reported a 30% drop in trust levels of British banks between 2007-2011 to just 16%! Moreover, banks' brands tend to be less loved than other popular brands. In a recent UK study on BrandLove, Apple came top of an index of 52 well-known brands with a score of 85%. The best a retail bank could manage was 12th in the ranking, and that was First Direct, an online bank (albeit part of HSBC), at 65%. Bank brands suffer from an emotional deficit – they rate quite highly on rational measures but very poorly on emotional engagement: they have poor personalities!

Clearly, there is much work to be done in the decade ahead, to claw back trust and win people over in terms of customer engagement, satisfaction and experience. Retention and loyalty strategies will be boosted when and if banks can interact in new and better ways with customers. Given this, it comes as a surprise to see banks doing so little in terms of innovation. In 2000, the word 'innovation' was mentioned an average of 1.2 times in the annual reports of America's Top 10 banks. By 2006, 'innovation' got 6.5 mentions. But by 2009, it hardly appeared at all with only 0.3 references, on average, per report.

Of course, it can be argued that internet banking, direct banking, mobile banking, online bill payments and the like are all innovative offers – but the point is that these have been a consequence of technologies invented elsewhere, rather than a direct result of banking ingenuity. Meanwhile, rather than stamping out creativity, regulations have actually forced change on banks. The same-day payments revolution came about because of regulators.

DEVELOPING WORLD AND FRONTIER MARKETS

…whilst less of an issue in the developing world…

In the developing world and frontier markets, the local, national banks enjoy a much stronger, positive image. They are not seen as responsible for the collapse of the global economy, for a start. They have built up long-term trust; a recent survey of 20,000 Asian consumers revealed that some 81% of consumers in these emerging markets wanted to deal with a local bank institution (source: McKinsey, 2011).

This gives local banks a huge advantage over foreign-owned banks in exploiting local market potential. This will not change much over the decade. Whether it be Indonesia or India, the national champions have the biggest ATM networks, the kids savings accounts and local business and political contacts. In some cases, local banks also have the legal right to offer certain basic banking products that foreign banks do not. In Singapore, for example, compulsory pension contributions have to be invested in recognisable funds which are only available through local banks. This is not to say that more cannot and should not be done by banks in the developing world to engage with consumers, particularly in light of the intense competition from mobile carriers.

In the developing world and frontier markets, the local, national banks enjoy a much stronger, positive image

...innovation is the key to re-invention in both worlds

So looking ahead, in order to address the image problem, retail banking in the developing, and in particular the developed world, will have to become more successful in reinventing itself, through:

More targeted product offers: reaching customers through 'pyschographic' marketing rather than product usage patterns or life cycle related tactics.

Increased focus on the unbanked: more active appeals to, and offers for, the 'unbanked' – in both developing and also developed worlds.

More offers to engage younger clients: an orthodox tactic of getting them whilst they are young, OCBC bank in Singapore is making a committed attempt to understand Gen Y (those people born during the 1980s and early 1990s) better and appeal to their motivations and behaviours beyond the financial sphere.

Initiatives to create win/win deals with the local retail community: for example, by offering a collection point for goods bought with their credit card.

Better clarity around the online interface: Kiwibank is a prime example of what can be done when a bank dedicates itself to providing a customer-oriented on-screen presence.

More banking around ethical principles: green banking is one area, but more social, inclusive banking is another. A true community bank which knows its customers, cares for its clients and gives loans to local people (whereas a centralised system might not).

More banking around Islamic Shariah finance: i.e. where all trading, loans and investing have to involve real assets and avoid gambling-style speculation. The Central Bank of Bahrain estimates the size of Islamic finance globally at $1.5 trillion and Moody's have suggested this could eventually grow to $5 trillon with a growing participation of London, New York, Paris, Tokyo and so on.

Increasing interest by banks in managing intelligence: information about money has become almost as important as money itself. As customer data becomes the key battleground, banks will need to reposition themselves as safe-keepers and interpreters of data. The worry is, that if banks do not, others will. Tesco a supermarket-turned-bank, uses food shopping patterns to predict the probability of loan defaults. How many banks currently can employ this level of analytics? Meanwhile, Amazon, Apple, Facebook and Google have built their businesses around information leadership. When they turn their ammunition towards money, as inevitably they will, banks indeed will need to watch out.

Implications for Real Estate

1. Impact on Branch Numbers

Huge rationalisation of bank branches in prospect in developed markets

DEVELOPED WORLD

The end of the big branch network…

The age of the big bank networks in the developed world is drawing to an end: there are fewer customers wanting to visit branches, too many staff and too many inefficiencies. We predict that as many as 50% of branches in networks may be declared obsolete in their current form in the developed world by the decade's end.

The fact of the matter is that much of America and Europe is over-banked due to big legacy networks built at a time when internet banking was a thing of science-fiction. In France, it is not uncommon to find a village of 4,000 inhabitants with 5 or 6 bank branches. America alone has 8,000 bank institutions (although this is substantially down from its peak of over 14,000 in the mid 1980s). Competition is so dense and consumers liking of online so intense, that one American operator was seeing an average of nine customer branch visits per hour. No wonder branch closures followed.

The problem of too many branches has been compounded by industry consolidation which has left many merged banks with catchment overlaps and full throttle cannibalisation. Britain has seen twenty core branch networks in early 2008 reduce to just 13 today, with the top six accounting for over 90% of the market. Clearly a gradual clean-out is on the horizon.

…but contraction will be slow and steady

But don't expect the branch network to disappear entirely by the end of the decade. For some time to come it will be a convenient drop-in service for the local population, an important branding tool, an information/training touch point. Meanwhile, in pure financial terms, many of the biggest banks simply have too much depreciation left in their branch assets and contingent liability on their balance sheets to engage in wholesale disposal strategies. Too much of retail banks' existing business model is built around branches. A steady run off in branch numbers is therefore the highest probability for the next few years.

Over the medium term, many banks will simply synchronise the timing of branch closures with lease expiries. However, we will see an accelerated closure programme over the second half of the decade once mobile banking really gets a hold of consumer behaviours and further asset depreciation leads to a ramping up of the disposal strategy.

The age of the big bank networks in the developed world is drawing to an end

Meanwhile, the arrival of new banks in a marketplace will also give rise to some physical expansion

Not all domestic banks will downsize…

It is worth adding that not all developed country banks will be downsizing. We will see some brave banks investing to build their bank network. Take Chase in America. They have been targeting 500 branch openings per year. Part of the logic of this will be to drive higher account penetration by having a larger network of much smaller branches in a State like California. Some financial modelling sees incremental deposit and revenue opportunities in this 'coverage' approach.

…and new market entrants and supermarkets will provide some growth…

Meanwhile, the arrival of new banks in a marketplace will also give rise to some physical expansion. In Britain, newcomers Metro Bank, NBNK, Virgin Money and Tesco are all seeking to expand their physical branch networks.

Hypermarkets could offer a particular threat to retail banks over the decade, since they have a powerful distribution channel already in place and could leverage their existing hypermarket locations. High traffic flow, strong brands, robust customer loyalty, capabilities in handling transactions and payments, expertise in database management and consumer targeting – all these skillsets and more would make any hypermarket a formidable banking operator, should they choose to invest. So, coming soon, the Bank of Walmart? Certainly Walmart's current financial services offer which provides alternatives to traditional checking accounts, particularly to the 'unbanked' in the USA and Mexico, seems ominous for the banks.

…as will banks from developing countries

There is also likely to be more overseas banks in the developed world by the end of the decade, following the Chinese banks' recent forays into Europe. And pursuing other opportunities in other Asian countries, Latin America and Africa. Developing countries in general are seeing deposit growth far outpacing loans growth and this is spurring on exploration of new revenue streams. However, the banks are not going to rush into overseas expansion due to the continued potential in domestic markets, and possibly pressure on capital, but also due to lower short term returns and higher opportunity costs in developed markets. The global journey will be undertaken, but only through a process of 'learn, diversify, then grow'.

2. Impact on Branch Networks

DEVELOPED WORLD

Remaining branch networks will be reconfigured

A key question is how the remaining branch networks in the developed world will be configured going forwards. The quality of the retail banking networks is mixed, to say the least. A typical bank's portfolio varies enormously across size, location type, catchment type, traffic flow and state of fit-out. Unfortunately, these variations are not often the product of strategic portfolio management i.e. the biggest branches are not always in the biggest catchments or found on the highest footfall locations.

Here, we will see a number of potential solutions being experimented with:

More convenient banking: including more ATMs, more 'kiosks' in high traffic flow zones (transport hubs, Malls), premium banks in business districts/parks. In the future, being in close proximity to the right customers will matter more than a prestigious façade, so we can expect more banks on, say, the second floor of an office building and tiny branches serving the local pedestrian flow.

More segmentation: some banks will try to segment customers and channels. Branches will focus on selling to high value customers, whilst low value transactional customers will be 'guided' to ATMs and direct channels. We will, eventually, see entirely cashless branches.

Hi-tech branches: other banks will focus on hi-tech branches minimising staff and even servicing sophisticated client needs through videoconferencing. For example, the Bank of Moscow is rolling out videoconferencing technology and giving customers access to call centre staff 24 hours a day. This model is seen as particularly relevant for banks with small and/or remote branches.

A hub and spoke combination: more commonly, some banks will try to combine both approaches above, in a hub and spokes approach. Highest quality face-to-face advice for more sophisticated banking products, will be available in the premium 'flagship' branches in cities. Smaller, local branches will be low on staff but give access to added-value services via video link.

Greater flexibility: As in retail, we can expect to see some banks adopt much greater flexibility concerning banks' physical presence and 'pop-up' access strategies and flexi-leases will be developed. More drive-thru' banking, anyone?

Digital technologies will increase data storage requirements

In both the developed and the developing worlds, digital technologies will be supported by ever larger, ever more powerful, and ever more expensive datacentres. Future location strategies for datacentres will therefore be, potentially, a bigger headache than for either head office or branch real estate. Data centres are hard to locate (near energy hub, in no-fly zones etc.) and are getting larger. The most probable response is a co-locate route whereby a third party manages the datacentres on behalf of the banks.

3. Impact on Banking Environments

DEVELOPED WORLD

Quality of banking environment will improve…

In addition to the networks, the retail banking environments in the developed world often leave a lot to be desired. Some company boardrooms can be accused of benign neglect of their banks' physical environments - some designs date from the 1970s and many lack the polish of their retail neighbours on the high street or in the Mall.

Over the next decade, banks will improve the design and fit out of their properties, which often compare very unfavourably with their retail neighbours. They will deploy a higher quality of materials and workmanship and aim to deliver a more consistent, branded look and feel. Citibank Japan, for example, launched its 'Smart Banking' branches in 2010, drawing inspiration from Apple stores amongst others. Nevertheless, by decade's end, banks will still lag mainstream retail in terms of quality of fit-out and retail theatre.

The move to a 'cashlite society' over the decade and the relative move away from physical cash and coin, will trigger still more changes in branches. Since the size and configuration of a retail bank branch traditionally has been conditioned upon the number of teller points at the counter, radically fewer cash and coin transactions will inevitably reduce branch size further. Branch design will continue its shift from counter focus to ATM focus. Also, expect the flagship branches of the future to offer more visible staff, released from behind counters, out on the banking floor (using versatile tablet technologies and interacting more with clients).

Swedish bank Jyske seems to want to be: 'the best coffee shop in town that also does banking'. Another European bank is planning a progressive new fit out, aiming to bring domestic elements to the banking hall, allowing customers to feel comfortable and unpressurised. Charles Schwab, meanwhile, is trying to replicate Starbucks as a Third Place and ING has also introduced a café ambience in some branches. Could Starbucks move into banking? In theory, anyone with an existing and loyal customer base could do so, subject to being granted a banking license.

Some banks have also experimented by dedicating some branch space to financial training clinics (e.g. Australian and New Zealand Bank) and others have allowed customers to come in and use the banking hall as their office – a kind of serviced office for the local business community.

…as banks follow the retail model

All told, banks have to become more like retailers, in the fashion of Metro Bank which speaks of 'customers' not 'account holders', 'stores' not 'branches'. And just like retailers who now focus on the wellness of their customers, the winning banks will be the ones dedicated to restoring the financial wellbeing of their beleaguered customers.
Banks moving into coffee shops and vice versa. JVing with coffee shops to provide enhanced products and services a path for the future?

Implications for Real Estate

1. Impact on Branch Numbers

Opportunity knocks, but dice stacked against western banks

DEVELOPING WORLD AND FRONTIER MARKETS

Opportunities for expansion…

The bank branch saturation that we see in the developed world will not occur in the majority of the developing world and frontier markets. The geographical, logistical constraints of much of the developing world, in conjunction with the technologies now available to banks in these geographies, and the advanced market position of non-banking competitors (mobile operators, Walmart in Mexico etc.) mean that having 'a branch in every town' is an unrealistic prospect.

Having said that, the developing world is where banking is going to be evolving the most over the next few years, and this will have a subsequent knock-on impact on bank branch numbers. Using McKinsey Global Institute analysis, which compared depth of financial products with per capita GDP, the following key countries have significant room for banking growth: Indonesia, India, China, Egypt, South Africa, Morocco, Brazil, Mexico, Ukraine, Turkey, Russia, much of Eastern Europe, Chile, Saudi Arabia. By contrast, those banking markets which are more saturated are those in the developed world – US, Europe, Japan – but including also, South Korea, Singapore and UEA.

…with India standing out

India in particular is hugely under-banked, and the market is now ripe for development. The last three decades have seen a significant increase in the size, spread and scope of activities of banks in India as its focus has changed from class banking to mass banking. For the sector as a whole, the last 10 years has seen an 18% growth in return on assets with every single year recording rising profits.

But the future promises to be more buoyant still. According to McKinsey, by 2017, the average consumption of rural India will be the same as urban India in 2005. The consequence will be huge increases in savings to the banking system and scintillating growth in consumer credit. Meanwhile, according to Boston Consulting Group, India's mortgage and wealth management business will grow ten times by 2020! Standard Chartered even predicted recently that India would become the world's third biggest economy by 2030.

In this context, India's banking landscape will change immensely and some predictions suggest the scope for 40,000 additional branches and 160,000 additional ATMs! These seem like over-estimates, given that Indians' traditional liking for bank branches might wane once mobile banking becomes firmly established. Nevertheless, the dynamic will be driven by the India government's push for more financial inclusion. Thus, the Reserve Bank of India has told banks that they will get authorisation to open branches in Tier 1 and 2 centres only if they also open branches in Tier 3-6 centres. Furthermore, they warn that at least 25% of all openings should be in un-banked rural centres.

Despite the potential rewards, expansion into the developing world and frontier markets remains challenging for western banks

Expansion strategies need tailoring…

However, despite the potential rewards, expansion into the developing world and frontier markets remains challenging for western banks. Each emerging economy is unique and solutions have to be customized across the value chain – product, distribution, sales and servicing strategies. Regulatory risks vary and so does the technological platform. One estimate by Bank Systems and Technology is that overseas banks have only been able to import between 30-40% of the mature-market technologies to emerging markets. Local stakeholder knowledge is also vital and under-estimating this learning curve over the next decade will end up with banks harming their brands' image.

…with caution the watchword for western banks…

The next decade will continue to see cautious expansion, with many institutions picking niches (often involving speciality products targeted at expatriates), consolidating them and only accelerating once they are regarded as quasi-local with embedded local processes and cultures. One Western bank in China, for example, is growing very sequentially at a rate of just three branches per year per province.

In a counter trend, we can also confidently expect some western banks to retrench from developing countries as balance sheet difficulties at home lead some to off-load their more distant networks. One way or the other, the decade will be rich with deal making and we will certainly witness further pack shuffling and international consolidation.

…enabling some Asia Pacific banks to target regional growth

On the other hand, banks like Australia's ANZ are making considerable inroads to becoming a "super regional" bank in the Asia-Pacific region through a combination of organic expansion and aggressive – but disciplined - acquisition. For example, in 2009 they took advantage of RBS's financial troubles to acquire its Asian retail, wealth and commercial bank businesses.

ANZ's regional accent is matched by Singaporean bank DBS. With 50 branches in China, an expanding network in Vietnam, a recent Taiwanese HQ and various wealth management initiatives in India, this is another bank focused on becoming a leading financial services group in Asia.

In a similar way, Indonesia's Mandiri bank is opening cautiously in China and Malaysia and plans to be one of the biggest banks in South-east Asia by 2020. It is being helped by further liberalisation of the Malaysian financial sector – an important prerequisite to any regional roll-out strategy.

Implications for Real Estate

2. Impact on Branch Networks

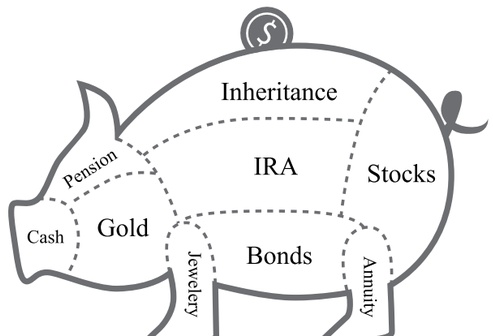
DEVELOPING WORLD AND FRONTIER MARKETS

Competition for space makes expansion tricky.

In the developing world, the questions about branch strategies and formats are as relevant as in the developed world, but will be placed in the context of ambitious - and tricky - roll-out programmes. Banks here are often finding it tough to fulfil their expansion strategies. For example, in first-tier Asian cities, there is strong competition for space on the High Street or in principal shopping malls. It is not unknown to find ten banks competing for the same unit in a new shopping centre scheme. The marketplace is dynamic and needs rapid decision-making. Nor is it uncommon to find a local 'hub and spoke' strategy scuppered when a lease review on the hub leads to branch closure. Security of tenure is far from guaranteed. Meanwhile, in secondary locations, foreign banks also struggle, faced with 'mom and pop' landlords who are unimpressed by their overseas credentials.

In essence, the problem expansionist banks are facing is the same as retrenching banks: it's about the fundamental branch model. Ideally, expanding banks want to be in prime locations next to retail consumer brands but just do not have the pulling power, the turnover nor the image to impress developers and investors. Therefore, the key question going forwards in Asia and South America is: what are banks going to do to make their branches more relevant and attractive to investors and landlords? Some of the solutions are in this Report and many management teams will have to deliver more successful formats and service solutions as the decade rolls forward.

Banks here are often finding it tough to fulfil their expansion strategies



Conclusion

We hope that this report provides some insight into where retail banking is going internationally, and what the knock-on effects are likely to be for real estate in developed and developing markets.

We have covered in this report the key drivers of change impacting the retail banking market; namely the increasingly savvy and mobile customer, the game changer that is technology, and the need for re-invention in order to regain lost trust.

In part, the answer to all these challenges will come from technology and innovation. Little more than a decade ago, most retail banks feared the internet. When they finally took the plunge, the results were positive. Now it is becoming ever clearer that the future belongs to those that are nimble and far-sighted enough to embrace future technology in all its forms.

Banks will continue to require physical space, but the emphasis on bricks is diminishing; and the physical space that remains will change both in form and function. The future is undoubtedly multi-channel.

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Front cover image of Virgin Money store, 98 King Street in Manchester, Virgin Money Press Release 2012.

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