GET FIT: SHINING A LIGHT INTO THE BLACK BOX

ZERO-BASED EVERYTHING (ZBX) FOR BANKING
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Banks find themselves in a difficult position: Against a backdrop of poor profitability, meager growth, and ceaseless regulation, they face new competitors attacking different parts of the banking value chain. And they are part of an evolving marketplace that will require them to become digital banks both inside and outside.

Accenture believes that to make feasible the leap to becoming a digital bank, banks must first become the best version of the legacy bank most of them are. This effort will produce what we call the “Future Ready Bank,” a simplified, profitable business that is manageable and agile enough to be transformed and that generates the funding required to fuel the leap to a digitally-native bank. See Sidebar: Return to Strength: Becoming a Future Ready Bank

RETURN TO STRENGTH: BECOMING A FUTURE READY BANK

While banking and financial services firms have spent a great deal of time, energy, and resources talking about becoming digital players, it’s important to be clear-eyed about where they currently stand in terms of this transformation. We believe the industry is still in the early innings of the game and that to make the leap from the existing legacy model to the full-fledged digital model is beyond the capabilities of the vast majority of banks.

The majority of banks remain legacy banks at their core. Indeed, it’s difficult to imagine how they might make the leap from their current state to becoming truly (i.e. outside and inside) digital banks. This is also why the measures outlined in this paper are applicable to banks that don’t have a profitability issue because of the benign conditions in their specific markets (e.g. Canada, Australia, some Asia-Pacific countries). To go fully digital, firms must first optimize their existing models to increase profitability—the fuel needed to develop the infrastructure and systems of the digital bank.

Our view is that between the status quo and the bank of the future is a “Future Ready Bank” with the following high-level characteristics:

- Cost/Income ratios of around 40% and a return on equity of about 15%, generating funding to invest in transformation
- Simplified and more transparent business, operating, and cost models
- Cultural shift to solving for clients, business, and shareholders (cost culture, service culture).

Getting there does not involve blowing up the business; rather, it means making the business simpler, more transparent, and more manageable. It also doesn’t mean waiting to use new technologies. In fact, becoming the future ready bank will require accelerated adoption of key technologies, such as analytics, robotics, artificial intelligence (AI), cloud computing, and the adoption of radical approaches toward efficiency and costs.

What does this mean? It means taking the bank as it is and making it profitable enough to invest in the future, transparent enough to manage effectively, and streamlined enough to evolve rapidly.
Cost has been a priority issue in banking for some time. For the past 10 years, banks have been trying to cut costs (and at the same time digitize their operations).

But traditional cost-cutting efforts have failed to deliver improvement on the necessary scale. The savings to date have been incremental—in the 10% to 15% range, if that. The stark reality is that what's needed is a transformational reduction of more than 30% (See Figure 2, below).

Moreover, banks' cost-saving efforts have been disruptive and damaging, driven almost entirely by across-the-board headcount reductions, rather than by targeted and purposeful strategies. As a result, some of the cuts have been to valuable and productive elements of the business.

The struggle to address costs is symptomatic of an underlying set of issues, which must be tackled to create the Future Ready Bank:

- **Complexity** – most banks have extraordinarily complex systems and process structures at their core
- **Huge central functions** – most of the complexity in banks' business and corresponding costs (55%-65% and more) resides in shared functions (such as Operations and IT), making it hard to relate processes and costs to specific business activities
- **Data** – the absence of agreed-upon, actionable, and robust data providing a “single view of the truth” makes it difficult for senior management to get its arms around operations
- **Management focus** – for most senior managers, large parts of the cost base are “somebody else’s problem”
- **Culture** – cost as a topic is seen to be about squeezing a little more out of different parts of the value chain. In a proper cost culture, it would be about how and where the bank deploys its main means of production: Money.

### FIGURE 2.
**Archetype: UKI/Continental Europe**

All figures in GBP billion (unless otherwise stated)

<table>
<thead>
<tr>
<th>Total Cost Variation</th>
<th>-37%</th>
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Source: Accenture
None of this is new. The reason why these issues have proven intractable, we believe, is strongly related to a set of organizational and cultural conditions at the core of most banks, that we call the “black box” (See Figure 3). The black box refers to the large part of a bank’s costs, functions, processes, and activities that are not directly related to or attributable to any single line of business. These are mostly central functions that have grown organically over many years, managed by leaders who are often incentivized by formulas that reward size of empire.

These functions have, of course, been squeezed as part of past cost-reduction programs. What most banks haven’t been able to do, however, is challenge what is done in these functions. That’s largely because the cost base of the black box is complex and opaque, and no one is truly incentivized to make it simpler and more transparent. Given this, the complexity and costs persist, constituting a significant obstacle on the way to becoming a profitable and agile bank.

We believe it is necessary and possible to shine light into the black box, shift the culture, and achieve cost savings in a way that minimizes the disruptive effects while still delivering cost reduction on the required scale.

To put banks on the path to optimization, senior management needs to shift to a mindset where everything can be challenged and where the goal is to unravel the processes and complexities of the black box.

This shift needs to be driven from the very top. This drive, however, is not about cost reduction targets but about a shift in culture and ambition. The key is to move from a culture in which employees feel that cost reduction is not their problem or at best an inconvenience, to one in which they take ownership of cost and complexity and ensure that everything can be, and is, challenged.

To do so, however, senior management must use its influence to establish a culture in which visibility, transparency, and ownership of costs are the goals of the organization, at every step and level.
A RADICAL FORENSIC APPROACH TO COST CAN MAKE VISIBLE THE ACTIVITIES AND THEIR OWNERS

Cost Transparency: The Solution to the Problem is in the Problem Itself

Paradoxically, the very costs that are so hard to shift—those that reside in the black box—hold a key to fixing the problem. At an atomized, granular level, costs are the footprints of the activities that form the black box. If a bank wishes to structurally change, simplify, and create the conditions for sustained cost management, it can do that by looking at the granular cost data and invoice, purchase order, and HR data.

A radical forensic approach to cost can make visible the activities and their owners (i.e. the parts of the business that cause the cost) while showing how cost taxonomies (what things are called and how they’re booked) obscure the data—and what needs to be done to create a taxonomy that makes costs and cost ownership more transparent. This sets the foundation for disentangling the complexity of the black box, establishing a shared taxonomy of costs and a universally agreed-upon view of data that can be used to challenge costs (for example, in a zero-based approach).

While artificial intelligence (AI) and analytics can speed up such a journey, it is still far from easy. It may be necessary at times to start the journey with cultural change and introduce a mix of general, mid-level, and deep (yet localized) granularity. This will yield results and build credibility, if done properly. But to achieve a leap change and lay the foundations for embedded and continuous cost management, working your way up from the most granular level of the general ledger is still the best approach to achieving visibility.
REDEFINING A TAXONOMY OF COSTS

This atomic approach will usually create sizeable quick cost reduction wins as indisputable wastage becomes visible. More importantly, by redefining and changing its cost taxonomy, the bank can create structures and mechanisms for continuous management of the cost base moving forward. Once the taxonomy is in place, visibility becomes a non-issue, because data is now organized properly. This then allows banks to create a closed loop of continuous and ongoing improvement, supported by a proprietary set of categories, processes, and levers. This closed loop allows for significant (+25%) and sustained cost reduction.

At the same time, the resulting transparency provides a strong foundation for strategic decisions, as businesses and their true economics are understood front to back. This provides a fact base for evaluating and planning new business models, divestitures, infrastructure changes, automation, outsourcing, and the like.

This may strike one as overly ambitious, but Accenture has done just this by building market-leading capabilities that shine light into the black box at the heart of organizations. Beginning in the Consumer Goods sector, and now in other industries—including a growing number of financial services clients—Accenture’s Closed Loop/Zero-Based (ZB) methodology is a proven, radical, and very powerful tool for corporate transformation.
Accenture’s Closed Loop methodology has two initial steps we believe are of fundamental value in and of themselves: visibility and ownership. The basic idea is that it’s impossible to manage what one doesn’t own or understand, and that one can’t take ownership for or understand what one can’t see.

**Visibility**

Visibility brings light into the black box by bringing together data from the General Ledger, HR and AP systems, invoices, and other data sources to create a rich dataset that categorizes costs in a meaningful way and clarifies cost ownership. It provides management with a front-to-back value chain view of the organization, costs, and headcounts tied directly to business line and revenue base. (Figure 4: “The Black Box—Turning on the Light with Closed Loop Methodology.”)

The effort required to achieve such forensic visibility is significant, as hundreds of millions of data items must be enriched and categorized. The use of innovative resourcing models such as offshore centers—and, increasingly, artificial intelligence (AI)—enable us to illuminate the inner-workings of very large, multinational businesses in two months. Other approaches we use can achieve significant results in even shorter time frames, but only a forensic approach can lay the foundation for embedded, sustained visibility.

As discussed above, visibility establishes a common taxonomy of costs. Working with clients over the years, our experience has been that significant parts of the cost base (often 15%-20%) are incorrectly categorized, resulting in data that is confusing and that consequently is not seen as meaningful by senior managers. Visibility corrects this, often also identifying substantial quick wins in the process.
Ownership

Ownership means moving from a state in which no one feels truly responsible for 65% of the cost base to one where someone is responsible for most if not all of the cost base—normally in a matrix of ownership involving business line and cost category management. As set out above, this creates the conditions for challenging not only what something costs (price), but whether it needs to be done in the first place (consumption). Bank leadership can make such ownership concrete by creating a framework for rewarding managers based on successful cost management. Arguably, clarifying cost ownership represents the greatest shift in improving a bank’s ability to manage itself.
CREATING A SOLID FOUNDATION FOR CHANGE

Experience has shown that visibility and ownership represent revolutionary steps in an organization's ability to transform itself. They establish a foundation of fact, transparency, and ownership/accountability on which strategic actions and interventions can be devised, based on a proper understanding of the functions, processes, and business affected.

Banks have conducted efficiency and change initiatives, often at significant scale, in the past decade. But in the absence of the foundation provided by visibility and ownership/accountability, these initiatives are exceedingly difficult—and often end in failure.

Viscosity and ownership provide a solid foundation for business change, including:

- Business rationalization where not only revenues, but also full front-to-back cost base, are taken out.
- Simplification and digitalization of a business, front to back.
- Evaluation of outsourcing options.
- Cost reduction initiatives, including Zero-Basing Budgets, Organization, Supply Chains and more, under a set of approaches we call Zero-Based Everything (ZBX).

...BY WAY OF LEAPS, NOT INCREMENTS

ZBX

While concepts behind Zero-Based Budgeting (ZBB) have been around for a while, our experience shows that the ways they have evolved and been applied can deliver significant improvements to organizational simplification and alignment, cost reduction, and business agility. "Zero-Basing," as used here, aims for leaps rather than incremental changes.

The powerful shift is to start from zero, with a blank sheet, rather from what is, and build up to a view of what should be. Critically, to do this ZBX needs management to get behind the process. ZBX, according to a CEO whose company applied the approach, requires a “maniacal focus from the top.”

Most ZBX projects are usually initiated by the visibility and ownership phase discussed above. That said, notwithstanding the limitations set out above, projects can be initiated with value targeting and Zero-Basing as well.
REALIZING SAVINGS OPPORTUNITIES

VALUE TARGETING

Value Targeting quantifies the savings potential based on top-down benchmarking and bottom-up (value lever) analysis to define total benefits as well as the specific savings initiatives for each cost category.

On spend, it uses operational data to dissect costs into price and consumption, and maps them against industry benchmarks and best practice. This identifies the savings potential and enables trade-off discussions as well as driving savings through smart policies. Similarly, it applies organizational benchmarks to identify areas for simplification and define the distinctive capabilities required to succeed in the marketplace. For example, for marketing expenses, value levers are identified by analysing consumption and price separately; e.g., in terms of consumption, spend is analysed looking at factors such as strategic alignment, consistency with the marketing plan, make vs buy, global asset adoption maximizing local re-use and adherence to global policies. In terms of price, factors analysed include consolidation of agencies and “fit for purpose”, de-coupling of creativity from production, use of techniques such programmatic media buying, etc.

Value Targeting is typically conducted jointly with client leads for each cost category (“Cost Category Owners”) to ensure that ambition and recommendations are aligned with and supported by the business.

THE POWER OF ZERO-BASING

As noted, the concept of Zero-Basing has been around for a long time. In our methodology and approach, however, Zero-Basing derives its power from combining the blank sheet with a negotiated challenge process to build a target budget, organization, and distribution model. The negotiation between category and business owners starting around the “should be” view has proven to be a very powerful tool to embed the future outcome in a way that the top-down targets used in traditional cost reduction simply can’t.

To summarize, two factors drive Zero-Basing:

- Starting from point zero—a position where there is no spending, no headcount, and no activity—changes perspectives in powerful ways
- The negotiated outcome is owned by the leaders, ensuring ownership/accountability.
The shared, transparent, and universally understood taxonomy of costs established by this method creates the foundation for embedding and sustaining a fundamentally improved level of cost transparency, ownership, and management at the heart of the bank. Having management go through this process forces them to take ownership. In creating constructive tension between cost category owners and business line leaders, the conditions are set for continued management of cost and activity in a way that traditional cost transformation programs cannot provide.

See Case Study: ZBX in Action.

CASE STUDY

ZBX in Action: Driving Business Value through Closed Loop ZBS for Marketing at a Global Bank

This global bank was struggling with double-digit growth in its marketing costs. The growth in marketing spend appeared uncorrelated to the way the business was evolving, and was therefore hard to justify. Moreover, there was a view that investments in offline and online marketing were not aligned to the bank’s priorities and objectives.

Complicating the bank’s ability to manage costs was the fact that less than 40% of total marketing spend was linked to a purchase order. Most of the spend was already aggregated in the finance system, usually because it came from other geographies or group entities or else because there was no link to a purchase order.

The opaqueness of the situation made it hard to pinpoint marketing’s return on investment (ROI), as well as the overall effectiveness of its campaigns.

The bank and Accenture launched a Closed Loop/ZBS program with the objective of:

- Making marketing more efficient by measuring cost per acquisition (CPA) and thereby ROI
- Enhancing the productivity of spend (shifting non-working to working)
- Rotating the marketing investment to digital in line with the Digital Transformation journey of the bank.

The project was run with the phases of the Closed Loop methodology:

Visibility and Ownership
Full bottom-up visibility was conducted across the bank, bringing visibility at a granular line-by-line level to the nature and ownership of different kinds of marketing spend. In addition to finding unaccounted-for spend, the Closed Loop/ZBS visibility phase revealed that nearly 10% of spend linked to a purchase order and more than 25% of spend linked only to an invoice were incorrectly classified in the GL. In the different geographies, marketing spend was shown to vary considerably in terms of adherence to policy, company strategic objectives, and effectiveness.

This phase also set out an accountability matrix with specific global and local roles per sub-category.

Value Targeting & ZB Design
Every penny of marketing spend was challenged to ensure full alignment to business and brand priorities. Guidelines for each category—media, agencies, sponsorships, production, and events—were defined in keeping with global best practices and benchmarks. The team developed a ZBB budgeting tool for marketing and digital sales, and deployed ZBB methodology by building the actual marketing and digital sales budget in more than 10 countries from the bottom up, managing both price and consumption levers.

The Outcome
The project reversed a history of year-on-year 15%-plus increases in marketing spend by delivering an equivalent reduction (effectively over 30% reduction on the cost trend line). Additionally, the project delivered a double-digit increase in working spend, and a near 50% increase in the firm’s digital marketing spend.

The method has since been embedded in marketing’s booking and budgeting processes, supporting continuous optimization—as well as giving the firm the ability to manage their marketing ROI, partnerships, and digital marketing effectiveness.
ZBX is a demanding and radical transformation effort that requires more than directive leadership and cross-business engagement to create sustainable change. Banks need to ask themselves: Do we prefer operating in the dark or are we prepared to embark upon fundamental and sweeping changes?

**Achieving Change**

Banks have struggled to build and sustain the capabilities and culture needed to return to strength around profitability, culture/ethics, and growth. From a cost perspective, this struggle is manifested in the high cost/income ratio, a low return-on-equity and, crucially, the severe constraints on the ability to invest in future growth. Traditional approaches have caused great pain with limited gain.

We believe that banks can achieve the step change required through a management culture that takes responsibility for all costs—and is prepared to challenge everything—empowered by actionable, granular-level data views of the interplay of cost/risk/capital.

Accenture’s Closed Loop/ZBX toolkit and experience can create the cultural, procedural, and data conditions required to return to strength, helping banks do so in a fraction of the time required by traditional cost reduction programs.