

# Mortgage Finance International: The Open Plan

by Andrew Porteous

## MARKET BACKGROUND

Financial services markets in the United Kingdom are among the largest and most competitive in the world. They have witnessed significant turbulence over the last decade and continue to be shaped by forces of change which together have led to an increasingly competitive environment and further industry consolidation. In order to flourish in highly dynamic markets, financial service providers need to develop and implement strategies and organizational structures that improve their competitive position and allow them to react quickly and with innovation to exploit changing market circumstances.

Some of the most significant pressures faced by U.K. personal financial services providers have included the following:

- Margins and commission rates have been under severe downward pressure, a process that has been accelerated by technology, particularly the advent of the Internet, with consequent disintermediation and increased price transparency.

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For mortgage banks, such as Woolwich, whose balance sheets and income flows were dominated by mortgages and retail deposits, the problem of margin erosion has been particularly significant as these products were increasingly adopting the characteristics of pure commodities, with competition primarily focused on price. The stock of high margin balances, the "back" books, were rapidly being replaced with "thin" margin new business, with the chum of business being historically high, reflecting the intense nature of competition.

- **New Entrants:** New entrants, such as Egg (owned by Prudential), have been able to capture a significant share of business flows in recent years. The successful new entrants have often adopted business models, supported through the application of new technology, with more flexible pricing structures than traditional suppliers and without their relatively expensive infrastructures and distribution channels. The emergence of new entrants placed a premium on management teams of traditional suppliers being able to manage rapid change and on increasing the efficiency of their operations.
- **Consumerism:** Consumers are increasingly sophisticated and educated about

financial matters and are more willing to seek competitive rates and move between suppliers. Moreover, technology has made available to consumers a vast array of information on financial services products that facilitates comparison and enables searching on criteria chosen by the consumer.

It was against the background of these market pressures, and their expected further escalation, that Woolwich began in the second half of 1997, following conversion to bank status (having been a mutual building society for 150 years), to develop the Open Plan concept. The senior management team, recognizing that the existing "mortgage bank" business model was ultimately unsustainable, began to sketch out the key elements of a customer proposition that had the potential to transform our business and its future profitability. Woolwich would use its relative lack of scale, as a medium-sized bank, and perceived by analysts as a distinct issue for Woolwich long term, to its advantage by being quicker to market and organizationally more flexible than our larger competitors.

## THE CONCEPT

The Open Plan concept developed from a challenge by Woolwich's chief executive, John Stewart, to think about what customers

wanted from financial services but on the premise that banks, as we currently understood them, hadn't been invented! We were effectively working with a clean sheet of paper to design the bank of the future.

For example, we asked why a customer should have to pay a higher rate of interest for borrowing on a credit card or personal loan than they did on a mortgage for purchasing their home. If there was sufficient equity in the property, we concluded, shouldn't all borrowings attract a lower rate of interest, regardless of what the money is borrowed for. We wondered why customers who normally used the telephone or Internet to contact their bank should not automatically have access to the same range and quality of service at a branch of the same bank. Also, why did banks treat long-standing customers as if they had no memory of them; the first thing they ask customers to do when taking out a new product is to fill in another application form!

We determined that if we were to start up a new service to help individuals manage their money it would not do any of these things. But rather the new bank would be built around the way customers wanted to control their financial arrangements now and in the future. Moreover, we recognized that consumers did not demand financial products and services for their own sake, but rather that they were a means to an end, i.e., to allow them the lifestyle that they aspired to.

So we began to create Open Plan. To be sufficiently different to create a viable customer proposition, Open Plan would need to incorporate the following features:

- **The customer in control:** The customer should feel that they could take control of their own finances. A current account should provide a hub for Open Plan with sweeping facilities to other accounts.

Customers should be able to specify a minimum amount to be maintained within their current accounts, with any excess funds being swept automatically to a target savings account daily. Up to 12 savings pots should be available to customers, to name as they chose, which reflected the way they thought about savings, e.g., a separate pot labelled for a holiday or a new car. Customers with an Open Plan mortgage should have the facility of obtaining a further advance simply by writing out a check.

- **Accessible:** A fully integrated service allowing customers to contact us and transact through whichever channel they wished and at times which were convenient for them. A customer should be able to ring the call center in the morning (or use the Internet) to transfer funds between accounts, and in the afternoon visit a branch where the assistants have access to systems that let them know these transactions had taken place earlier in the day. Essentially, this meant the provision of a 24/7 service available through a full range of channels, including the traditional, physical outlets and the emerging electronic options.
- **Financial planning and advice:** High quality financial advice should be available to customers based on a thorough understanding of their lifestyle aspirations. Wherever possible, the service should reduce the perceived complexity surrounding financial products and remove the "hassle" factor for customers of dealing with a multitude of companies to meet each specific need.
- **Tangible benefits:** Not only should the proposition be profitable for Woolwich but also there should be real tangible benefits for the customer. One aim was to aggregate balances, for example, to allow savers the optimum rate across all

their savings and to allow borrowers to consolidate debt at mortgage rates.

- **Seeing the whole picture:** Allowing the customer to see the whole of their financial arrangements with Woolwich on one consolidated statement.
- **Customer service:** Very high standards of customer service would need to be consistently available across all the ways in which we could touch the customer.

How could we develop and deliver such a ground breaking service, which undoubtedly would require significant management focus and investment, while continuing to run our current business at levels of profitability demanded by the market and our shareholders? Essentially, we needed to be highly resourceful in the deployment of new technologies to enable us to begin the transformation of our business.

#### A TECHNOLOGY-LED SOLUTION

As it was our vision that Open Plan would become our core business through time, it was essential that the selection of technology (and the technical architecture) was capable of providing a long-term solution. The system would need to be able to support 24-hours-a-day operations, requiring reliability and robustness, but would also need to be scalable to cope with a rapid growth in customer numbers. It would need to be able to assimilate the emerging electronic channels quickly, without the requirement for any major and potentially lengthy redevelopments. Moreover, the system would need to supply the same customer data across all the channels.

To support these objectives, Open Plan was created with a three-layered architecture. At the front end are the systems that interface with the channels, while at the back end are the legacy account processing systems

(based on a number of applications running on an IBM mainframe, including Hogan software). However, the key to making Open Plan an integrated multi-product, multi-channel proposition was the development of middleware. This middle layer, running on NT servers, communicates between the other two layers, using business objects as a common "glue." The key advantages of middleware were that it enabled product developments to take place once and be effective across all channels, the architecture facilitated the rapid adoption of new channels and from a customer perspective "anytime, anyhow, anywhere" banking would be delivered in a seamless way. Through the year 2000 as major competitors were establishing "stand-alone" Internet banks, the integration facilitated by our middleware clearly differentiated the Woolwich offering.

A customer database was also a key component of the overall design as customer information would be central to our objective of creating enduring and profitable customer

relationships. It would enable our organizational focus to move away from single products to meet specific needs to providing customized financial solutions. In practice, this meant that the data warehouse needed to be populated with customer data from a large number of disparate sources, providing a single view of the customer across the organization. By employing techniques such as data mining and segmentation, value added customer information could be created, providing meaningful insights into customer needs and aspirations.

A simplified Open Plan systems architecture is shown in the following diagram (see Figure 1).

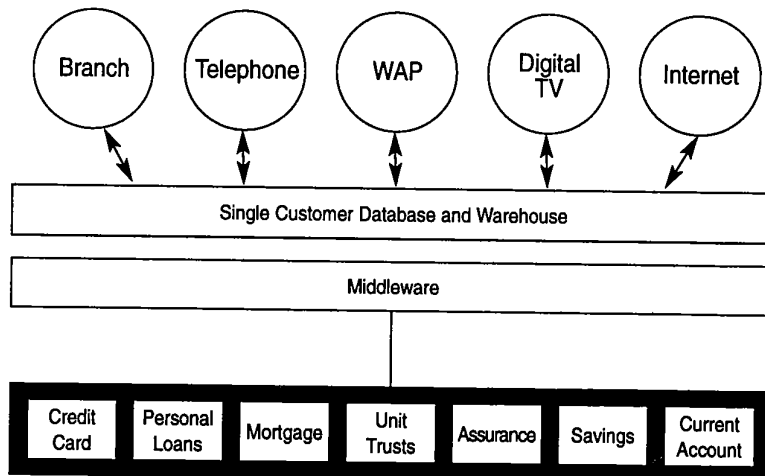
Our systems solution not only met our requirement to deliver Open Plan, but it also enabled the continued use of the heavy historic investment in our legacy systems while providing the flexibility to respond quickly to changing market conditions and customer requirements.

Woolwich worked with a number of integration technology partners, including AIT and Microsoft, over a number of months to develop the key elements of the enabling technology architecture. Our objective at this time was to get Open Plan up and running quickly so that we could conduct a pilot to test the underlying proposition, the sales approach and the functionality and robustness of the underlying systems. In the highly competitive and dynamic markets in which we operate, speed was of the essence if we were to establish clear space between ourselves and our competitors and achieve market leadership.

**THE PILOT**

The Open Plan pilot started in late 1998 with an initial offering to staff, allowing us through their feedback to improve the customer experience. The Open Plan call center in Clacton, which was to be the principal operational facility for enrolling and servicing Open Plan customers, was opened. Shortly afterwards Open Plan was piloted in a small number of selected branches. The sales of Open Plan were primarily through advisers called personal finance managers (PFMs) who undertook a fact find to ascertain the requirements of prospective customers. This process proved to be time consuming and by June 1999 some 6,000 customers had been enrolled into Open Plan. Experience from these early phases of the Open Plan pilot indicated that more efficient distribution would be necessary to increase the volume of new customers and reduce the cost of acquisition. Therefore, in the Bristol area (in the southwest of England) over the summer months, the sales process was refined so that more cost effective sales staff were used and, as a consequence, customer numbers rose sharply to 25,000 by October. This was supported by adopting a modular approach to marketing Open Plan (with product bundles suitable for customers with savings and investment needs, require-

Figure 1 Open Plan Architecture



ments centered around borrowing, or the "full service" version).

The pilot proved that the Open Plan proposition would appeal to the mass market and that with an average of three or more products per customer, the value of an Open Plan customer was around 65% higher than a typical "classic" customer. Consequently, the Woolwich board agreed to an investment program of £125 million over three years, with the aim of acquiring 2 million Open Plan customers by the end of 2002.

**ALIGNING THE ORGANIZATION**

However, we also recognized that transforming our business through Open Plan necessitated a fundamental review of our operations and organization. Consequently, in late 1999 a new customer-centric organizational structure was introduced, which split the organization into three main areas (customer strategy, production and channels), supported by central functions and service providers. The structure was developed around the principle that the customer should be at the heart of

our operations, hence, it supported the capabilities which would allow Woolwich to build a real understanding of the needs of our target customers. It also facilitated the achievement of operational excellence, through technology-led, efficient common processes and the development of accessible banking through a fully integrated, multi-channel distribution capability.

This customer-centric structure is shown in Figure 2.

As a major United Kingdom public liability company (a FTSE 100 company), a key priority for our senior management team was a comprehensive communication program of our strategy to the analyst community and institutional shareholders. It was essential that they fully understood that the changes we were embarking upon were essential for the long-term success of the company, although in the short term profitability would be diluted as a result of the scale of the investment required to reinvent our business. Against a background in which analysts were generally downgrading forecasts for

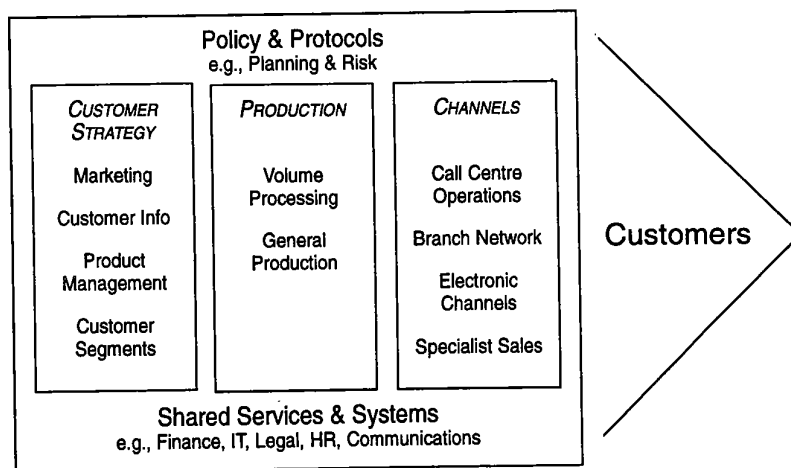
mortgage banks (principally as a result of expected margin erosion), Woolwich's Open Plan was regarded as a sustainable new business model. However, they recognized, as we did internally, that the major challenge was moving from defining the strategy and running a pilot to full-scale implementation. The year 2000 was to be all about delivery.

**ROLL-OUT OF OPEN PLAN**

The key target for 2000 was to have at least 500,000 Open Plan customers by the end of the year. Starting the year at around 44,000 customers meant that we had to attract on average nearly 40,000 per month to the proposition. Clearly, this meant a step change was required in our ability to attract customers and then subsequently to process applications quickly and efficiently. While the capabilities of the Open Plan call center had been geared up over several months, it was decided that we would look to an experienced outsourcer to process Open Plan applications, but once set up as an Open Plan customer, our own call center would assume responsibility for servicing their on-going requirements. The key advantage of an outsourcer was that it had access to facilities and staffing that would be capable of being more flexibly matched to the peaks and troughs of demand, hence, maintaining the high levels of customer service that was a key part of the Open Plan offering. The company we chose to work with was Ventura, one of the U.K.'s largest providers of call center facilities.

To ensure that Open Plan received the necessary external exposure, Woolwich embarked on a major advertising campaign, involving a number of media, including television, radio and newspapers, to extol the virtues of Open Plan. The advertisements build upon the successful theme of "you are with (Woolwich) or without" and the campaign significantly raised the profile of Woolwich and Open Plan brands. As new fa-

Figure 2 Customer-Centric Structure



ilities and features were introduced into Open Plan (some of which were groundbreaking in U.K. retail banking) during the course of the year, these were highlighted in advertisements, press releases and presentations. Key among these were the introduction of access to the service via WAP phones (April), the Open Plan Offset Mortgage (June), the first operational offset mortgage in the U.K., and the addition of digital TV (September).

Internally, we needed to ensure that Open Plan received the highest priority if we were to achieve our targeted number of customers. An extensive change management program and internal communications supported the roll-out of Open Plan, with the aim of ensuring that every member of staff knew they had an important part to play. Regular updates of performance against our Open Plan targets were published across the organization, together with Open Plan regularly being the topic for discussion at staff meetings.

So how did we do? Well, by the end of the year we had exceeded our target and had some 540,000 Open Plan customers. The build-up of customer numbers over the year is shown in Figure 3.

Moreover, we successfully attracted customers from our targeted customer segments into Open Plan and maintained product penetration above three products per customer. This would prove to be a good base upon which to build for 2001, with our expectations set at having well in excess of 1 million Open Plan customers by the end of this year.

**HOW IT WORKS**

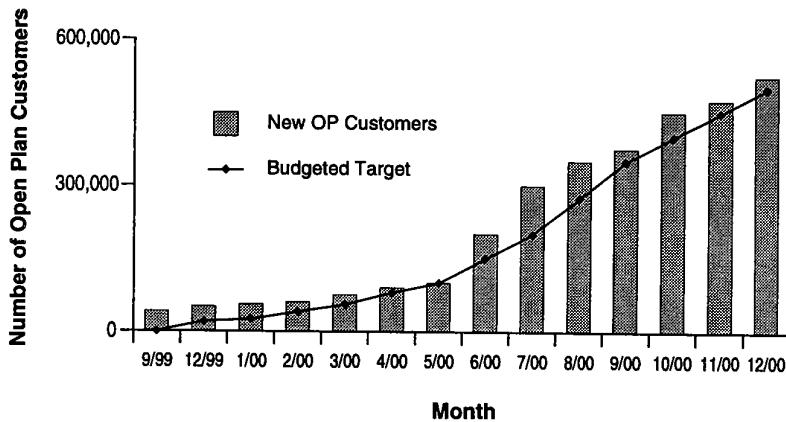
Open Plan provides real benefits to customers through automated facilities such as sweeping, aggregating and offsetting. Sweeping allows customers to control their finances by sweeping monies between accounts, either through a pre-agreed rule (such as current account to be maintained

with a minimum balance of, say, £200 with the excess being swept to a target savings pot) or for ad hoc occurrences arranged through the call center or one of the web-enabled channels (such as a part redemption payment for a mortgage). Aggregation provides customers with an interest set on their total savings balances, despite the fact that these holdings may be split across a number of separate savings pots.

However, it is the offsetting facility that perhaps illustrates best how customers can benefit from an organization taking a more holistic view of their financial relationships. The Woolwich Offset Mortgage, which was the first operational offset mortgage available in the U.K., allows savings and current account balances to be offset against the balance of the mortgage, used to determine interest paid and calculated on a daily basis. This allows the customer to reduce the cost of the mortgage or even pay it off earlier. A simple illustrative example is shown below:

£65,000	Initial Mortgage
-£ 7,000	Savings
-£ 500	Current Account
<b>£57,500</b>	<b>Offset Mortgage</b>

Figure 3 Open Plan Customer Base



Mortgage interest is calculated on the offset balance of £57,500 and while the customer does not receive interest on the offsetting balances, he will be better off as the mortgage rate is higher than that paid on savings and current account balances. In April 2001, Woolwich introduced a new variant of this product (Offset Together), which allows the savings balances of family members in Open Plan to be offset against an individual's mortgage.

**WOOLWICH WITHIN BARCLAYS**

Open Plan proved highly popular with customers and we soon recognized that it had the potential to be played out on a much

larger stage. While Woolwich could have remained an independent and successful mid-sized bank, we had always been open minded about consolidation opportunities, provided that any partner shared our business philosophy and value was created for shareholders.

Barclays, one of the U.K.'s major clearing banks, had conducted a strategic review following the appointment of a new chief executive, Matt Barrett (formerly of Bank of Montreal), in 1999. One of the key conclusions was that to fulfill its retail financial services strategy, through increasing its share of customers total financial services activities, required a more meaningful presence in the U.K. mortgage market.

Initial talks between the respective chief executives highlighted that both organizations held similar views about the future of banking and, indeed, their operations were highly complementary. Clearly, Open Plan was one of the principal attractions of Woolwich to Barclays, together with the quality of our management team and our highly productive IFA operation. Following more detailed

work, involving a small group of senior executives, a business plan was developed which quantified some £240 million per year (after three years) of synergy benefits from integrating the two businesses (subsequently increased to £400 million per year to be achieved by the end of year four).

A recommended offer from Barclays, representing a significant premium on the prevailing Woolwich share price at announcement, was accepted by Woolwich shareholders and in October 2000 Woolwich became part of the Barclays Group. This transaction allowed some of the value implicit within the roll-out of Open Plan to be crystallized for Woolwich shareholders. The combined entity possessed a customer base totalling 16 million, over 2,000 branches and was the leading provider of e-finance in the U.K. Woolwich was part of an organization which possessed the necessary scale to afford the on-going investment to keep Open Plan a market leader.

Within Barclays, the Woolwich brand and customer experience has been retained. One of the key income generative synergies

has been to develop Open Plan for sales using Barclays brand and distribution, and this is due to be launched in autumn 2001. In total, we have set a target of attracting some 5 million Barclays/Woolwich customers into Open Plan by the end of 2004.

#### CONCLUSION

Open Plan has proved extremely successful for Woolwich and will be the platform upon which our future profitability will be based. It is popular with customers, offering a level of accessibility, functionality and convenience that has not historically been available within the mass market. Open Plan has also received a great deal of external praise and recognition; for example, it was voted the "Best Shareholder Value Strategy" in the BT/Institute of Financial Innovation Awards (December 2000).

Our key challenges are now to continue to enlist large numbers of customers into Open Plan, to ensure that the proposition remains at the forefront of customers' minds despite competitor "noise" and to continually add new and innovative features to maintain our competitive advantage.