Banks are scrutinizing their processes the way manufacturers do—by looking for inefficiencies

For banks in need—getting more from Lean Six Sigma

By Peter Guarraia and Andrew Schwedel

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Peter Guarraia, based in Los Angeles, is a partner with Bain & Company, and a member of the firm's Performance Improvement practice.

Bain partner Andrew Schwedel is based in New York, where he leads the firm's Financial Services practice for the Americas.

Editorial team: Lou Richman, Elaine Cummings
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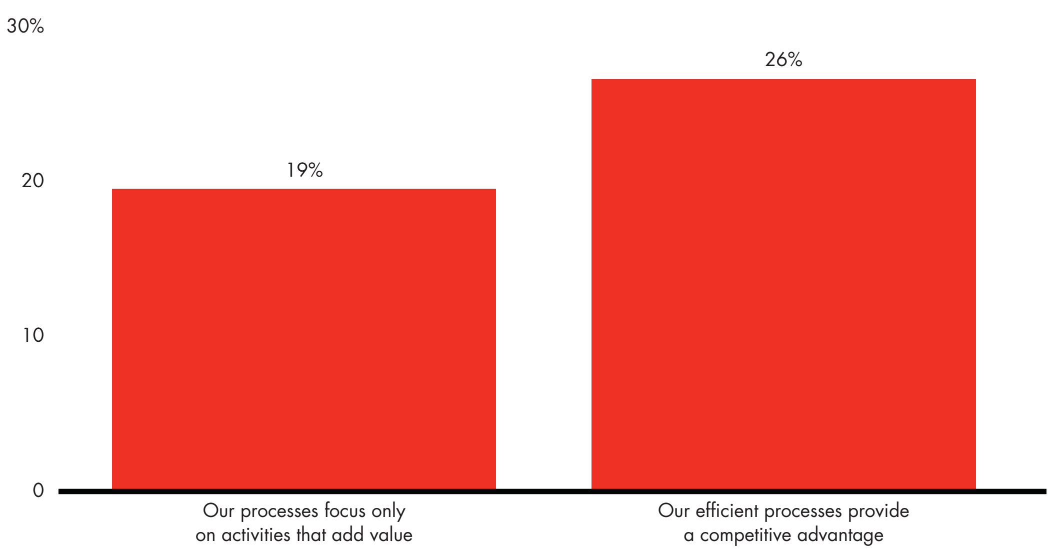
Scorched by the subprime-lending crisis and facing a faltering economy, banks are feeling the heat to eliminate business process defects to put performance back on track. Many financial services companies will turn to Lean Six Sigma, the popular tool developed by manufacturers to capture cost savings and productivity gains on the factory floor. From North Carolina to Quebec and South Korea, banks are beginning to use Lean Six Sigma to hone growth strategies and boost customer service. Bank of America defied skeptics who doubted the technique's applicability to a big services company by reporting more than $2 billion in benefits from its extensive Lean Six Sigma efforts. BMO Financial Group's Bank of Montreal credits its Lean Six Sigma work with freeing up $55 million in cost savings it can reinvest in growth. In Seoul, Shinhan Bank applied lean techniques to integrate operations following its 2006 merger with Chohung Bank and became one of Korea's leading commercial lenders.

Yet there are many lenders who complain that their Lean Six Sigma experts—known as "black belts"—simply haven't delivered. In a recent Bain & Company survey of senior managers at 184 companies, fewer than one in five said their Lean Six Sigma efforts were focused on the right activities. Only just over one-quarter felt that their process improvements were giving them a competitive edge. (See Figure 1.)

While Lean Six Sigma can be excellent for remedying obvious maladies like assembly-line problems, it is less proven as a tool for relieving sources of pain lurking within business processes. Too often the black belts treat all problems, big and small, with the same approach and fail to prioritize improvements that will make the biggest difference.

Figure 1: Most companies are not satisfied with their Lean Six Sigma efforts

Percent of companies that strongly agree



Source: PI Diagnostic Survey, n=184

We've found that financial services companies with the best results begin with an upfront diagnostic X-ray. Knowing where to focus *before* unleashing the black belts can make all the difference. Performed by a small advance team, the X-ray consists of three steps:

1. **Mapping the value stream:** The X-ray team maps primary processes to identify the biggest opportunities to trim costs by reducing wasted time and materials.

2. **Benchmarking performance:** The performance of each process is measured against internal and external benchmarks to gauge shortcomings and identify improvement targets.

3. **Prioritizing improvements:** The X-ray team determines which process improvements will yield the greatest results when black belts are deployed.

Here's how two banks have used the diagnostic X-ray to get better results from Lean Six Sigma.

A bank supports its growth strategy

When a major Asian bank wanted to take advantage of a residential property market slowdown to grow its commercial banking division, it recognized that it would need to overhaul its credit processes at every level in order to handle a larger volume of complex loan applications. Value-stream mapping revealed major trouble spots, including a lack of uniformity in loan application approvals that resulted in delays and errors that required costly rework. Instead of adhering to decision rules derived from long institutional experience, credit officers too often made lending decisions based on personal judgment. Also, all loans—large and small—had to move through the same initial layers of approval, causing more delays.

The diagnostic team then compared loan-approval processes across different bank branches to find out how long, where, and why applications were stuck. The benchmarking exercise revealed potential improvements by more broadly applying the best local practices. For example, the team discovered that one branch expedited loan application decisions by simply assigning a credit officer to work alongside loan managers on the bank floor.

With value-mapping and benchmarking results in hand, the bank prioritized a short list of high-value opportunities, the third element of the diagnostic X-ray. By focusing on one of these—developing a fast track for processing lower-risk loans—the Lean Six Sigma black belts delivered concrete results. Nearly half of all loan applications now get expedited treatment, and errors requiring rework have dropped by 25 percent. As a result, new business is fueling growth at 2.5 times the market.

A merchant bank saves a merger

When a US-based merchant bank acquired its major competitor, management was divided on how to run the merged business. The vastly different business practices followed by the former competitors were fueling friction that was driving top talent out the door. Management deployed the diagnostic X-ray to build a consensus around how best to integrate operating practices and quickly identify top areas for improvement.

In the value-stream mapping phase, the diagnostic team compared loans that both institutions had reviewed to see how their different processes affected approvals. The map showed that while the merchant bank was better at assessing larger, riskier deals, its approvals took much longer. The acquired bank was faster and delivered better customer service—but its deals typically were smaller. The team's follow-up benchmarking exercise against competitors showed that the merchant bank had many unnecessary approval steps, which frustrated its best customers.

The team prioritized improvements by looking for quick, high-impact solutions that would help retain talent. At the top of the list was a loan-approval system with a fork in the path:

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Lower-risk deals take a simpler route, while harder deals go through a more rigorous, but standardized, process. The solution incorporated the acquired bank's speed and predictability with the acquiring bank's sophistication for handling larger deals, allowing the merged entity to accelerate approvals and increase its average deal size by 35 percent.

Before financial services companies rush to apply Lean Six Sigma techniques to squeeze out inefficiencies and mend broken processes, they should step back and, as these banks have done, take a diagnostic X-ray first.

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