



*cutting through complexity*

# Cultural (r)evolution

Cultural progress in banks

July 2015

Research collaboration

**bba**

The voice of banking







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Culture is always hard to define. However, when a bank's demand for growth is aligned with the long-term interests of customers, I think we will have reached our destination.

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Bill Michael

# A permanent cultural (r)evolution

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Banks are on the way to embedding a new sense of culture in their organisations, but still face public criticism as they have not yet found a way to explain the new sense of equilibrium between creating trust, generating returns and continuing to innovate. The drive for financial performance, without the balance of other attributes created a sense of imbalance within the system. Scandals such as the FX and Libor rates manipulation, are seen as being indicative of systemic challenges and all boards recognise the absolute need to address this criticism.

The hunger for financial results was not fully counterbalanced by a realistic appreciation of the risks involved in realising such goals. In their desire to become one-stop-shops, banks arguably placed their ambitions to sell a wider portfolio of products above the actual needs of customers, and the results were clear to us all.

Changing the one-stop-shop cross subsidised mentality has to be addressed. But how to penetrate the hives of blockages in the bank's own system? How can banks change their behaviour and mentality? How to make them think: Would I sell this to somebody I know?

Nevertheless, as this survey shows, the link between culture and negative conduct has been well acknowledged, with all the banking executives involved citing ongoing cultural change programmes within their organisations. This is not all that's happening. In a separate study of banking chief executive officers, 60 plus percent say they will devote significant capital to transforming their business models, and nearly 60 percent believe that their business and operating models will undergo their most rapid change in the next three years<sup>1</sup>.

Culture must be the epicentre of this (r)evolution, in order to create customer-centric organisations with impeccable ethical credentials, totally focused upon what is best for personal and corporate clients. Culture is always hard to define. However, when a bank's demand for growth is aligned with the long-term interests of customers, I think we will have reached our destination.

My experience is that many get it or are well on the way to getting it. Considerable progress has been made and leaders should be congratulated for their achievements so far. The journey is only in its infancy and the scale of change cannot be underestimated, as it impacts every aspect of banks' activities. However, at the same time they shouldn't lose sight of innovation – it needs to be the driving force when they design and price services, how they reward staff, and how they interact with customers.

I believe this paper makes an important contribution to a critical debate over the role of some of society's most important institutions. It would not have been possible without the participation of 21 senior banking executives, and I would like to thank them for giving their time.

## Bill Michael

EMA Head of Financial Services

KPMG

<sup>1</sup> Global CEO Outlook Survey, UK Banking data, KPMG/Forbes, July 2015



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Each organisation – whether large or small, established or new, UK or foreign – has their own perspective on culture, all view the moral compass of their organisation as core to the well-being of their operations and that of their customers going forward.

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Anthony Browne

# Introduction on the cultural dialogue

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In the immediate aftermath of the financial crisis, banking reform focused on enhancing the financial stability of banks and the financial system. Strengthened capital and liquidity standards, recovery and resolution planning and, here in the UK, ring-fencing. Banking supervision has been overhauled and the Bank of England given new macroprudential tools. The High Street has seen an injection of competition in more ways than one. And we have reached the point where international regulatory consensus is being reached on the final steps needed to address 'too big to fail'.

With the market conduct failures that came to light in summer 2012, the spotlight turned to conduct and culture. The Parliamentary Commission on Banking Standards (PCBS) sat for almost a year under the Chairmanship of Andrew Tyrie MP culminating in the Government and regulators accepting some 80 plus recommendations made in the Commission's report *Changing Banking for Good*. Many of these sit firmly in the statutory or regulatory space, such as the introduction of a criminal sanction for the reckless mismanagement of a bank, the reversal of the burden of proof for regulatory enforcement action and the replacement of the Approved Persons Regime with the Senior Managers Regime – all intended to enhance individual responsibility and in the process address what had been described as "the orient express defence".

Steps within the regulatory regime, however, can only take you so far in seeking to improve ethics and behaviour. This is why the BBA advocated the establishment of a new body – firmly within the industry space – tasked with raising standards of professionalism within banking. With the appointment of Dame Colette Bowe as chairman of the new Banking Standards Board (BSB) following a nomination process overseen by an eminent panel chaired by Mark Carney, Governor of the Bank of England, and Alison Cottrell as CEO, the new body is up and running, and will shortly open its doors for membership. The Fair and Effective Markets Review has now concluded and this will see the establishment of a FICC Market Standards Board to sit alongside the banking institution orientated BSB.

While the BBA can rightly be described as a 'champion' of this approach, we were equally clear in our evidence to the PCBS that the new arrangements had to be independent of the industry and the BBA as its representative body. We have therefore been clear that while the BBA can – and should – continue to support initiatives aimed at raising professional standards in banking we should mostly leave the question of how to take this forward to the new arrangements being put in place precisely for this purpose.

Which is where this report comes in. We held a dinner only a matter of months ago at which the topic for discussion was culture. We didn't define it and we didn't lead. All we did was put senior executives from across the banking sector into a room and invite them to discuss. And we came away with the strong sense that while each organisation round the table – whether large or small, established or new, UK or foreign – had their own perspective on culture, all viewed the moral compass of their organisation as core to the well-being of their operations and that of their customers going forward.

With encouragement and support from Bill Michael and his team we thought some of these perspectives were worth capturing in a little more detail and relaying back to participants and the industry.

## Anthony Browne

Chief Executive

British Bankers Association





# Executive summary

In the years since the financial crisis, culture in banking has risen up the agenda – for the media, the public, shareholders, regulators and for the banks themselves. In their 2015/16 Business plan the Financial Conduct Authority (FCA) highlighted culture as a key area of risk. There is widespread consensus that a cultural shift was and is necessary, and with external pressure for reform, in addition to self-imposed imperatives, banks of all shapes and sizes have made culture a key strategic priority.

In order to gain a deeper understanding of the progress that has been made in recent years, and the amount of work still to do, KPMG with support from the BBA has undertaken qualitative research, involving in-depth interviews with 21 senior banking executives. The interviewees represented banks from across the full spectrum of the sector, including custodial, wholesale, retail, investment and private banking services.

## Key findings

The research highlighted four key themes:



### 01. Culture remains high on the agenda across banks of all shapes and sizes, but not always for the same reasons

By force or otherwise, culture has risen to the top of the agenda. It is now frequently discussed at executive level and for many of the respondents it has become an explicit strategic priority. It is a clear focus area for those banks caught up in the mis-selling scandals of recent years. For the banks that did not face significant regulatory challenges following the crisis, culture is an important focus for other reasons, including being used as a vehicle by which they can differentiate their brands in the market, or to underpin new growth plans.



### 02. Banks have made considerable progress on their respective cultural journeys, but the more challenging work is yet to come

All of the banks interviewed are at different stages of their cultural evolution, and whilst many of the changes implemented to date have been challenging, the more difficult task of embedding the culture in all parts of the organisation will require the resolution of some tough dilemmas that will likely require changes to the business and operating model.



### 03. There is a need to establish robust metrics to help track and measure cultural reform – effective measurement of culture remains a challenge

Consistent with other recent research<sup>2</sup>, banking leaders recognise the need to establish measures that provide a rich picture of how culture is developing over time. Quantitative and qualitative metrics that adequately capture the nature of a bank's culture are hard to find, yet necessary to demonstrate progress to all stakeholders.



### 04. Building a sustainable culture for the future is a long game and to achieve it will require the next generation of leaders to resolve some very tough dilemmas

The key challenge for banking leaders is to identify the dilemmas that impact different stakeholder groups in the banking ecosystem, to develop a model that enables an optimal balance to be achieved between the needs of all groups, including customers, clients, staff, shareholders, regulators and society overall.

<sup>2</sup> New City Agenda, A report on the culture of British Retail banking, November 2014



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## What do the findings highlight?

The findings indicate that the importance regulators have placed on the need for cultural reform has been taken to heart in the boardrooms of the UK's banks. There is acceptance and acknowledgement that creating the right culture – one that places an emphasis on customer service and ethical behaviour – should be at the heart of running a successful bank and is critical to their future success.

There was strong consensus that culture needs to be led and shaped by the CEO, in the role of the 'Chief Culture Officer'. However, a top-down approach is only one half of the equation. Given the nature of culture, there was a clear recognition that a strong element of bottom-up engagement is also needed, to ensure all employees are inspired, empowered and incentivised to act as cultural ambassadors for the organisation.

The sheer diversity, unique character and history of each bank in our sample highlighted that banks are at different stages on their respective cultural journeys. The concept often reflected in the mainstream media, that all banks are facing the same cultural challenges, is clearly not the case.

We found that banks in our sample fell into three categories with regard to how they are thinking about culture.

### 1. Major banking institutions that have remediation activity ongoing.

This group included several of the institutions that were most severely impacted by the conduct-related scandals of recent times, and are consequently trying to drive cultural change in close alignment to the regulatory conduct agenda, whilst at the same time addressing low levels of staff morale and engagement.

### 2. Banks which emerged from the crisis relatively unscathed and have not required regulatory intervention.

Executives of these banks were also very focused on culture, but for different reasons. Either their attention was on how to protect the culture that had served them well through the crisis, and adapt it as required by the current approach to regulation. Or, their attention was firmly on growth, and therefore how they might nurture their culture and shape it in a way which enabled growth whilst respecting the regulatory and societal expectations of the moment.

### 3. New entrants to the market, including challenger and specialist institutions.

These banks were predominantly focused on how to protect and develop their culture – often seen as a genuine differentiator in a crowded and competitive market, during rapid growth. Also included in this category were the non-domiciled banks offering services directly to UK-based customers, as well as those using the UK as a hub for other international activities.

## What are the implications?

The scale, scope and complexity of the cultural challenge facing banks should not be underestimated and at the same time, cannot be uniformly applied to all banks. The banking crisis and subsequent scandals have meant that many institutions were blamed for the same mistakes. However each faces its own unique challenges, depending on past events and ambitions for the future.

Some of our interviewees felt that change could be realised in the short-term, whereas others felt change could take decades – “It will take a generation to genuinely change culture,” said one of the CEOs in our survey. This is consistent with the view of MP Mark Garnier, member of the PCBS. However, there is also a need for greater urgency as stressed by Martin Wheatley, Chief Executive of the FCA: “...for its own sake, as well as for consumers, it is an imperative for industry to reduce the frequency and scale of the problems it has encountered. And I do not think firms have the luxury of waiting a generation for that to happen.”

Likewise, those tasked with cultural reform need to look to the future as well as the present. Whilst there has been an emphasis on raising awareness of the importance of culture and running bank-wide culture programmes, there is a need to embed those changes in a way that supports the long-term viability of the institutions, so as not to stifle innovation and growth.

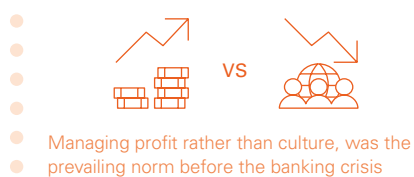
The forces of shareholder, regulator, customer, employee and general society expectation have set up a number of fundamental and underlying dilemmas that are making the next phase of culture change much harder than those that have come before. Only by realigning business and operating models to the needs of these diverse stakeholder groups can those cultural dilemmas be reconciled – and reform achieve its true purpose.

# From the inside: the progress of cultural change

Seven years on from the start of the financial crisis, and in the wake of the latest wave of regulatory fines for misconduct, this time for forex manipulation, now is an appropriate time to take a closer look at the topic of culture and ethical standards in the UK's banking institutions.

Through interviews with banking executives, we explored the topics of culture and ethics in UK banks. In particular we were interested in the insider view on the importance of the topic. How much of a strategic and operational priority is culture? And in the perceptions of progress – that is, how much cultural change has been achieved to date? We also gathered views on the next steps in cultural reform and the hurdles that will need to be overcome in order to satisfy the expectations of the regulators, shareholders, customers, employees and the banks' own leaders.

## Pre-banking crisis



## Initial aftermath



## Today



## A historical perspective on the problem

Many interviewees acknowledged, either on their own behalf or as regards the industry generally, that managing profit rather than culture, was the prevailing norm before the banking crisis. They concede that this led to some facets of the banking model being overly weighted towards serving the needs of the bank and its shareholders or employees, with outcomes for other stakeholder groups sometimes coming second. To some extent this continued into the initial crisis period, when banks focused on their immediate survival, becoming less risk-averse and working to ensure their operational viability and sustainability.

In the aftermath of the crisis, and amidst stinging public and media censure, came a realisation that poor culture led directly to poor conduct, and with the intervention of the regulators arose a new landscape of regulatory compliance against cultural characteristics and behaviours. From this point on, culture and compliance became inextricably intertwined.

Today, there is a universal understanding that culture, specifically, as it is reflected in conduct towards customers and markets, is the key to restoring trust in banking. Moreover, all banks understand that this must be a universal undertaking, as the crisis showed how the actions of a few can have a profound effect on the overall reputation and credibility of the many.

To that end, regardless of their history, brand proposition, culture and conduct before, during and after the banking crisis, all banking executives interviewed had culture programmes and activity under way – either to address cultural failings of the past or to drive the future growth strategy with culture and values at the core.

# The three phases of the cultural journey

We found that regardless of the individual circumstances of the banks in the aftermath of the financial crisis, not only were they all engaged in a cultural journey, but that journey comprised three distinct phases:



## **PHASE 1:** **CULTURAL AWARENESS**

The first phase began with campaigns and initiatives to raise awareness of the importance of culture, as a key driver of business outcomes, and evangelising it throughout the institution, with a clear 'tone from the top' set by leadership.



## **PHASE 2:** **TACTICAL CULTURAL INITIATIVES**

This was followed by more formal culture initiatives or remediation programmes focused on tactical changes and improvements across a number of areas such as HR, Learning & Development, Compliance and Conduct Risk Management.



## **PHASE 3:** **OPERATIONAL CHANGE**

The third and arguably most challenging phase is to ensure that cultural reform is both reflected in and reinforced by fundamental changes to the end-to-end business and operating model, including the design of products and services, the reward and incentive model for staff, interaction with customers, cost structures and pricing.

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## Where are the banks on this journey?

The majority of those interviewed felt their institutions had progressed through phases one and two and were now looking at ways to embed the required infrastructure, processes and behaviours to enable long-lasting change.

Yet whilst phases one and two required large-scale communications and engagement campaigns, often challenging and costly in themselves, phase three is seen to be more complex. It will mean in many cases, a cold, hard look at some of the core products, services and capital allocation decisions at the heart of the business model, in order to create a sustainable balance between benefit to stakeholders, clients and retail customers. None of those interviewed felt they had completed this third phase of the journey.

At the same time, it was very clear from our interviews that no two banks are on the same cultural journey, and the nature of the required change differs from firm to firm.

All interviewees accepted that the effect of the crisis and its subsequent shaping of the regulatory

regime has hugely influenced banking culture, for many, preserving aspects of their culture which have served them well – in some cases for centuries – is equally crucial to their future sustainability and the maintenance of their competitive advantage.

For other banks, there is a strong focus is on how they can replace the measures by which they used to drive business performance – such as sales incentives – with cultural measures and use the positive reinforcement of culture and values to increase productivity and profitability, whilst maintaining regulatory compliance.

In all cases, however, there was a universal agreement that regardless of the extra administrative burden, despite the difficulties of reconciling often conflicting commercial objectives, the banking industry is treating culture as far more than just a public relations exercise. As one interviewee pointed out, “A strong culture is not necessarily a differentiator... it’s a basic requisite.”



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Whilst phases one and two required large-scale communications and engagement campaigns, often challenging and costly in themselves, phase three is seen to be more complex.

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# What are the key messages?



## Key finding 1:

**Culture remains high on the agenda across banks of all shapes and sizes, but not always for the same reasons**

All executives interviewed for this piece stated that culture and ethical standards are a key focus for them individually, their peers at executive level, and for the organisation as a whole.

As one executive of a European bank described, "Culture has moved from being perhaps second to financial and activity-based performance, to being right at the top of the agenda." Similarly, an executive from an investment bank talked of how, "Culture has gone from not being a major focus to being one of management's most important focuses."

However we had a clear sense from our discussions that the drive to change culture had now taken on a life of its own, and had become – for many – an end in itself rather than a means to an end; culture has become a constant, rather than occasional, issue. In the words of an executive at a universal bank, "It's part of our day-to-day business life." This is true for those banks which have faced more challenging circumstances, but also for those which have not felt it necessary to change their culture but rather, are keen to protect and nurture it. As an executive of an international bank put it, "I would not say that the culture has changed but we are more careful how we reinforce and make it clear to the members of staff. Before, we could assume that they knew what would be acceptable, now we cannot assume any more."

For one of the new entrants to the market, culture remains high on the agenda for different reasons, with a strong focus on using culture to shape the organisation's internal and external identity. In the words of the respondent, "The values and culture of the organisation is one of our key competitive advantages... we're trying to create a values-based bank in a commodity market."

## The job is not done yet

From our interviews, there was some strong evidence of self-challenge and critique. We did not get the sense that executives felt the job was done. Some challenged themselves on the degree to which cultural change has been truly embraced at all levels in some banks. One interviewee, when asked whether all banks have embraced the need for cultural change, stated: "Yes, I wouldn't say embrace is right, but I think the whole of the banking industry has recognised the importance of culture change... I think there is definitely across the industry a recognition that it has to be different in the future."

One interviewee put it candidly: "What has changed is our ability to have the culture that existed before 2007. What I mean by that is we no longer have the operating platform from which people can do what they did. I can definitely say that we do not have the same culture in respect of risk taking that we did, but it's like putting a 70-mile-an-hour speed limiter on your car. We're not speeding, but does that mean we don't try and speed up but can't? I can't really judge that."





## Key finding 2:

**Banks have made considerable progress on their respective cultural journeys, but the more challenging work is yet to come**

Every organisation interviewed had made some progress on its cultural journey. From communications campaigns, to raising awareness of the importance of a strong culture, to implementing cultural improvement programmes that make tactical changes across a number of functional areas, there has been a great deal of action, not just pronouncements ‘from above’.

Making these changes has been challenging. One bank, for example, described the challenge of having to work with employees who were the most disengaged they had ever been, in the aftermath of the crisis. Another talked of how difficult it was to retain a sense of positivity, saying, “The problem is that the good banks, the good culture is so overwhelmingly drowned out, or shouted over, by the bad stuff.” However, awareness and engagement are in a sense, just the first steps in the foothills of culture change.

Banks are well aware that the next set of steps – over significantly more challenging terrain – are to develop a sustainable strategy that embeds the desired culture and behaviours at all levels of the organisation. In the words of one executive, “Our culture awareness programme has moved to a governance advancement programme.” Another executive, similarly, talked of entering a new phase. “You address those priorities and then you move more from tactical to strategic. We’re in that strategic phase now.” Yet in the words of that same executive “focus is evolving continually” as the regulatory environment continues to evolve, media scrutiny changes its focus and organisations themselves grow into their new cultural clothes. This makes it difficult to develop a simple vision, a clear strategy and a measurable activation plan when the goalposts continue to sway in the tailwinds of the financial crisis.

As one interviewee said, “I think there’s been a huge reliance on compliance and regulation which has its place, but you’ve got to change people’s hearts and minds. It’s happened to some extent, but I don’t think nearly profoundly enough.”

To really accelerate progress through the next stage of the journey, more fundamental business or operating model change will be required to instigate culture change. Ultimately, only when the products, services, business processes and underlying metrics are aligned to the desired culture and business objectives, will the benefits be fully realised.

This theme was also reflected in another interview, in which the executive described his bank’s cultural challenge as moving from an accountability culture and a rules-based approach to one of ownership and stewardship, in which the bank serves a much broader set of interests in society as well as the integrity and sustainability of its own financial ecosystem. For this to be authentic, employees need to feel that they have ownership and stewardship of something tangible, that even in the middle of the organisation, far from the coalface of customer service, but equally distant from the lofty heights of the boardroom, they can reach out and touch.

“You know, 150 years after the inception of an institution like ours, it’s actually there, the culture’s there. What we don’t necessarily do is have a habit in banks of practising our culture, reminding ourselves what our culture is, putting it on the walls. It’s important that you’re not doing culture because you’re trying only to satisfy the regulators or avoid fines. You’re doing culture because what you do is so important. Without having a culture, it would be ridiculous; it would be absurd.”



### Key finding 3:

**There is a need to establish robust metrics to help track and measure cultural reform – effective measurement of culture remains a challenge**

Everyone interviewed recognised the importance of measuring progress on their respective cultural journeys and had implemented their own way of doing so, including for example client satisfaction scores, Net Promoter Scores and employee engagement surveys. Yet none had yet developed a systematic approach that they were fully comfortable with. In the words of one executive, “Every time we have a culture session, that’s the question I ask, if the culture has changed, how will we know?”

Given the amorphous and intangible nature of culture, in all its emotional and metaphysical dimensions, this is hardly surprising and intuition can be a surprisingly good indicator of progress in the absence of set metrics. Culture, is after all, an outcome that is observed rather than a process in its own right, and is more complex than a formulaic scorecard. As one executive said, “Culture is about people, and how you make everybody do the right thing. It’s the way we do staff meetings, the way we tell our story, and it’s hard to put on a scorecard.”

Nonetheless, it is essential that banks establish criteria and quantitative and qualitative metrics to help identify changes in cultural attributes, and there are a number of data points that can be collected and collated to review the extent to which cultural change is being achieved over time. There is a significant opportunity for innovation, to establish core values, agree processes, collect data and analyse the quantitative patterns and procedural effectiveness into a simpler, more easily describable set of cultural metrics.

One banker referred to a raft of measures including “all of the normal HR metrics in terms of how long people are staying with you, all of the retention and absence and turnover, all of the conduct measures, from customer satisfaction through to complaints through to breaches through to everything that you would measure as a bank, which sums up our Balanced Scorecard.”

Another talked of a comprehensive flagging system integrated into the organisation’s HR, compliance, training and communications system, thereby ensuring that issues such as remuneration and promotion are aligned to culture.

In contrast, another took the position that first-hand experience is a more effective measure of culture than a defined set of metrics, saying, “We don’t rely on reporting, we believe it’s important to walk the patch, meet customers, talk to people and talk about the bank’s culture, and provide coaching and support. Given that we all embrace the bank’s culture and we all appreciate it, then when we identify areas of slippage, we take action.”

“ Many banks are starting to look at the richness of the people data that they hold to measure progress on cultural attributes. HR predictive analytics has a big role to play and real-time big data can provide powerful insights in areas such as trader surveillance. ”

**Jayne Vaughan**, Partner, KPMG

One thing almost all interviewees agreed on – at least when it came to conduct-related cultural measurement – was that the best arbiters of this were the customers themselves. All executives showed a passion for getting direct, regular and honest feedback from customers to inform their culture and to act as a yardstick to progress.



#### Key finding 4:

**Building culture sustainably into the future is a long game and to achieve it will require the next generation of leaders to resolve some very tough dilemmas**

As this research shows, and corroborated by a separate KPMG analysis of financial results in the UK banking sector, the industry is facing some steep challenges<sup>3</sup>. In the immediate future, many banks are facing an apparent dilemma which is on the one hand reducing risk taking, complexity of product and aggressiveness of sales, yet on the other hand, increasing profitability and return on capital.

For some, cutting costs or restructuring the balance sheet will be unlikely to get them to where they need to be in the eyes of their shareholders, as the regulators are constraining some of this activity, either directly or indirectly. Many see getting the culture right as a key to unlocking this value – that is creating a culture where people understand the right behaviours in a particular circumstance, which give the right balance of outcome for customers, shareholders and other stakeholders. If banks can achieve this, then they will have a robust yet flexible culture that can effectively resolve these tensions in the longer term.

This will have the added benefit of also helping to create a more positive internal environment for employees. Many employees were not personally responsible for, or involved in, events that led to the financial crisis and later scandals, yet they feel personally tainted. Working for a bank has, for some, gone from a source of pride, to something to hide.

Many of our interviewees highlighted the need to re-engage staff in a positive and purposeful vision for their bank, emphasising the crucial role they play at the heart of society. Others introduced the topic of how to train the next generation of bankers, and how they could begin to make their culture change sustainable by ‘designing it in’ to the career paths and training programmes.

There was a broad consensus that whilst some aspects of cultural change may take “three to five years” it will take far longer to fully embed the change, improve public opinion and return to a position of trust within society. One executive referred to it taking “30 to 50 years to return to a position of restoring trust” due in part to the “long tail” of scandal and mistrust.

At the same time, several banks acknowledge that culture cannot be ‘once and done’. In the words of one, “We’re never done. We are always learning.” Culture never stops. There will always be innovations and there will always be difficult challenges in the market and banks will continue to evolve and change. There will be new technologies. There will be new product services solutions. There will be new regulations. There will be new entrants to markets. There will be new competition. There will be disruption. There will be pressures.

“ UK banks spent £9.9 billion on remediation activity in 2014.<sup>4</sup> A painful reminder that customer-centric strategies are not implemented yet. Culture change requires fundamental change in areas such as capability development and re-design of career paths for future banking leaders to provide the breadth of view, understanding of risk management and an intuitive commitment to ethics and service. Only then can the sector fulfil its purpose to all stakeholders. ”

**Julian Morgan**, Partner, KPMG

<sup>3 & 4</sup> Benchmarking Report 2014, A paradox of forces, April 2015

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For the major banking institutions that are still in the process of conducting remediation programmes, culture can be used as a platform for renewal and reinvention, rather than simply a way of preventing the same historical issues from arising again. Likewise, organisations that emerged from the crisis relatively unscathed and those that have not required regulatory intervention, need to continue to develop their cultures aligned to regulatory requirements whilst placing greater emphasis on the opportunities that present themselves. New entrants to the market, including challenger banks and non-domiciled banks, will continue to use their distinct cultural identities to their advantage to attract new customers and clients.

David Packard of Hewlett-Packard once observed that, “Marketing is too important to be left to the marketing people.” In a similar vein, culture is not exclusive to the CEO or a select team of executives, nor is it confined to any particular type or scale of organisation. As one executive put it, “Culture is not a national thing, it’s not sector-specific and it’s not size-specific either. If you’re an organisation that focuses on customer service, you can do that in any sector and across any size.”

Rather, for culture to work, it has to change people’s hearts and minds and inspire everyone in the organisation to support and contribute to it in the long term, once the honeymoon period of the early stages of a cultural initiative is over. Maintaining this sustained energy is a key challenge: “It’s easy to launch and it’s easy to whip up an initial level of enthusiasm. Embedding it on a sustainable basis and doing that over a long sustained period of time is much harder.”

The next steps in the evolution of culture will need to consider the banking business model, getting to what one executive described as “the heart of the client lifecycle” and whether the existing operating model is still appropriate in the new paradigm.

Banks will need to consider how they make money through their products and services – and whether those products and services are congruent with the culture it wants, how it serves the customer or behaves in the market, and through which delivery methods and how it incentivises and rewards staff to achieve consistently good outcomes for customers and shareholders. Regardless of how far away employees are from the customer, despite organisational silos, processes, structures and incentives, employees must feel that the culture is their own and enhances, rather than constrains, how they work. One executive interviewed summed it up as, “For me, culture is about how we do banking. How do we ensure that we are delivering a brilliant and honest relationship with our customers and with our colleagues and with society as a whole in a way that is meaningful?” For that to work, everybody in the organisation must know their part, and play their part.

# Conclusion

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Through our conversations with a diverse range of UK banking executives, we have learned that progress is reshaping the culture of banking.

However, within the current paradigm, much of the cultural change that can easily be achieved, has already been achieved. Creating truly sustainable, ethical cultures will mean in some cases abandoning policies and practices that served banks well in the past. This will require some tough decisions for banking executives, as they look to create the culture of their institutions for generations to come.

Culture change will take years, perhaps a generation. Nor will it be finished then. Decisions made by banking executives today have the potential to shape the future success of their institutions. The banking leaders of today have a unique opportunity to create a cultural framework that will last a lifetime. Only by grasping this opportunity can banks provide the basis upon which trust can be restored in the coming years.



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The banking leaders of today have a unique opportunity to create a cultural framework that will last a lifetime.

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# Appendix:

Detailed findings  
across the  
banking spectrum

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# Major banking institutions

For many of the major banking institutions, the financial crisis, whilst having a profound impact, was not necessarily the start of their cultural journey. This came slightly later, with scandals such as PPI and Libor, or prompted by painful rogue trader losses.

These experiences have had two key consequences. On the one hand they have created a desire among leadership to improve the culture for the future, on the other they have led to regulatory focus that has seen cultural improvement programmes put in place with ongoing supervision. Regulation has had a profound impact on behaviour in banks. As one of our interviewees said: "Would we have done it to ourselves without regulation? Absolutely not. So in that sense the crisis has had a very profound effect on culture."

## How do the major institutions define culture?

- "The biggest challenge from a cultural perspective is to have people living and breathing that and not having to consciously think about, well, what would this mean for the customer? It just comes absolutely naturally"
- "My personal definition is that I try to conduct myself in a way that my mum and dad would not be embarrassed to read about"
- "Good culture in banking is where you can meet the responsibilities of your role both as an individual and as an institution in a manner which is effective, efficient and creates the right outcomes for all stakeholders"

## What example initiatives have been undertaken?

One major institution undertook a long-term programme to re-engage with employees, starting from one of the lowest-ever staff engagement scores compared to its peers across Europe. A UK-wide strategy was developed involving face-to-face communication, opportunities for employees to raise their issues and concerns and enabling management to act upon them.

Another bank described how a culture of escalation is emerging, with 'real context and challenge' around how to remediate and treat clients. This is side by side with a greater emphasis within the HR function of a review and recalibration of performance appraisals to encourage and reward behavioural change.

A large bank, which experienced a significant conduct-related loss, has instituted a 'challenge' initiative, whereby people are encouraged "to dig, to ask questions, to be thorough and be willing to take your colleagues on" without fear of repercussions and reprisals.

### What has worked and what has not?

The consensus among the major institutions is that action-based initiatives are considerably more successful than those simply based on communications. Being seen to ‘walk the walk’ and put culture into practice, particularly at a senior level, tended to lead to higher levels of engagement and adoption. Initiatives that change the working environment are the most successful of all. As one executive put it, “What we’ve really done is change the conditions in which people operate and that, in time, is what is going to change people’s behaviour and attitude and ethics.”

Whilst truth and reconciliation can be an effective way of creating a collective commitment to learning from the mistakes of the past and moving forward together, creating a climate of blame and fear is not. Internal workshops, when people were publicly held to account over behaviour that in the past was considered acceptable by the norms and culture of the time, were seen as unfair and unproductive.

### What progress has been made?

The majority of the major institutions noted progress in implementing cultural reform, largely because of the scope and scale of their reach and resources, in engaging both employees and customers and importantly, in their ability to demonstrate results on a grand scale, due to their large base sizes. As one executive put it, “It’s now very much more explicit about what those standards are and brought into more everyday language. So there’s been a significant change, certainly in terms of awareness, and all the research we do is that people have a very good understanding about what those values are and what they mean.”

### What challenges have been encountered?

Ironically, the challenges came from the same place as the advantages: that of scale. Many executives talked of the difficulties of embedding values into the everyday operations of the business, “so people are not just aware of them but they actually adopt them and practise by them”. As one executive described it, “The challenge is actually getting that across an organisation of tens of thousands of people globally and many thousands of people in the UK, getting them to adhere to that in a consistent fashion, day in day out.” One example of this is in recruitment – an activity that is by nature devolved lower down the organisation and in a large organisation is practically an everyday occurrence. Given that “who we hire and who we fire” can have such a profound effect on culture, many organisations gave this issue a very high focus.



## Unscathed survivors

Organisations that emerged from the crisis relatively unscathed and those that have not required regulatory intervention.

This group includes those banks that face increased regulatory attention due to the focus on culture in the sector. This is not necessarily due to past actions, but due to increased attention on the sector overall.

The cost of regulation and increased compliance has impacted these banks. One executive described how, “The crisis has had a very profound effect on culture... margins have been reduced, commissions substantially abolished... overall bonus pools have been reduced.”

For one of the foreign banks interviewed, the Senior Managers and Certification Regime requirements will impact their culture, saying, “We pride ourselves on our devolved structure, it has helped guide our business success from the mid-1970s. The regulator’s requirement for individual responsibility impacts culture.” There was a general sense among these institutions, as there was with the challenger banks, that culture is more than simply a matter of regulatory compliance, but at the heart of the bank’s operating ethos, relationship with its customers and employees and an important part of its vision for the future.

Whilst banks in the group are typically smaller than many of the major banking institutions, their smaller size does have its own benefits. “We’re on a scale where everybody knows everybody. I can get every member of my team in sessions of 250 people and talk to them about these things that are very real.”

### How do the ‘unscathed’ banks define culture?

“People should get up in the morning wanting to do what can be broadly described as being an honest day’s work. It doesn’t actually matter which industry you’re in, that should be why people get up in the morning. It’s no different in banking or investment management or anything else, you’re there in our industry to serve clients and you serve them honestly.”

### What example initiatives have been undertaken?

One bank uses its devolved leadership model as a platform to ensure that all staff “could really appreciate and understand that it’s their responsibility to look after the customer and do the right thing.”

The bank simply tells its staff “you must focus on giving the best service to the customer, the best advice” secure in the knowledge that that will build long-term relationships which will lead to long-term commercial success.

Employee engagement is a key feature of these banks’ cultural initiatives, with staff councils, forums and working parties which are run by members of staff, and people are encouraged to join. One bank in particular pointed to these groups as a key source of new ideas and fresh thinking, rather than simply a way of making it appear to be listening to employees.

In other banks, employees are even more engaged. At one bank, employees felt that their employer could be doing more for the environment, so they lobbied the board to sign agreements and memorandums of understanding that led directly to greater activity on the company’s behalf.

One bank interviewed holds client focus groups when it is planning changes or new initiatives, for example, to its online banking service or mobile phone app, invites their views and incorporates their feedback going forward.

### What has worked and what has not?

These smaller institutions generally find that applying their collegiate approach to doing business to their cultural initiatives results in high levels of engagement and adoption. As one executive described when asked how his staff feel about culture, “I think they would talk about ownership, empowerment and responsibility. I think they would talk about pride and the ability to make local decisions for individual customers.”

As with all the banks interviewed for this research, they pointed to the recruitment of new staff as a critical element of culture. In fact several mentioned how they had put much greater focus on the recruitment process in recent years, as a way of identifying and attracting people who share the same vision and values. As one says, "The interview process for us is vital, and we find if people don't fit the culture they leave pretty quickly."

Another recurring theme among these institutions was when the central management team facilitates and supports the branch network in a horizontal, rather than vertical, chain of command.

The requirements for individual responsibility through the Senior Managers Regime could prove challenging with the inherently collaborative nature and matrix model in many banking institutions. As one executive says, "Essentially what the regulator is actually asking us for is for everybody to be very clear about who's responsible for what. In reality, in a matrix organisation, that can be more than one person."

#### What progress has been made?

As far as these institutions are concerned, their culture was broadly right in the first place and did not need 'fixing' so the question of progress is a moot one. However, they did all understand the need to clearly articulate that culture and provide quantifiable means by which to demonstrate how it links to regulatory compliance. Several institutions gave examples of being able to 'prove' that their culture was compliant, as one executive describes a regulatory review in which traders were questioned in a spot check:

"They weren't going to tell us which traders so we couldn't prep them and they wanted to ask them questions. They did random sampling of our dealing room and no issues emerged from any of that. I was very proud of the floor and therefore the culture... People came up, took it entirely seriously, sat down with the regulator, answered the questions impeccably and it shows that somewhere along the line the message we'd been conveying had landed."

#### What challenges have been encountered?

The key challenge with these institutions has been the need to change the way the bank works, when, to the point above, they may never have received a regulatory penalty in the first place. As one says, "Some of the ways of assessing new clients have been quite onerous, and clients don't always understand regulatory requirements."

There was a sense that these measures were holding the bank back, making it less efficient, less competitive on an international playing field and causing unnecessary friction with staff who felt they were now being told they could not be trusted to make the right decisions for themselves.

“ Our recent survey showed that 70% of industry managers believe the new regime will drive greater accountability and improve the industry standards. ”

**Suvro Dutta**, Partner, KPMG





## New entrants

New entrants to the market, including challenger banks and non-domiciled banks offering services directly to UK-based customers, as well as using the UK as a hub for EMEA and other international activities.

This is not a homogenous group and includes a range of banking institutions, including those that have been carved out of legacy banks, foreign banks that have entered the UK market and the banking arms of wider cross-sector institutions.

Some of these banks are not constrained by legacy systems and processes and have been able to start with a relatively blank sheet of paper, which gives them the advantage that culture can be 'baked in, rather than bolted on'. Designed for a post-crisis world and cognisant of their competitive advantage relative to other, more tarnished institutions, these institutions are inherently more aligned to focusing on the customer and on service delivery. For some, particularly the retail banks, culture is seen as a key differentiator in a competitive and commoditised market; they have a decentralised infrastructure, empowered employees and processes and protocols that have more in common with the retail industry than with traditional banking.

### How do the new entrants define culture?

"A business that starts with the consumer and absolutely has always focused on doing what's right for the consumer and along the way doing some good for society. That's the fundamental philosophy."

"Culture is about how we do banking... how do we ensure that we are delivering a brilliant and honest relationship with our customers, colleagues and society."

### What example initiatives have been undertaken?

What is striking about the challenger brands, is that they have not looked to the banking industry for ways to differentiate themselves. Rather, they have looked to other industries, particularly retail with its tradition of service, devolved management structures and egalitarian, performance-based remuneration, for their inspiration.

One bank, for example, has created a flat reward and remuneration model based "unashamedly" on that of the John Lewis system of a bonus as percentage of salary, equally applied to all partners "that only rewards leadership and employees when we make a profit and when our customer satisfaction benchmarks are met."

Employee communications follow a similarly collaborative theme, with employee-led engagement forums tasked with solving business problems and helping to design new products as well as addressing 'softer' issues. In the words of one executive, "It enables a proper engagement between the executive team and people who are on the front line who see our customers."

“ Certainly our experience of talking to investors is that they absolutely buy into the point of difference that your culture makes. ”

Given the emphasis on people and customer service, it's not surprising that staff induction is a recurring theme. One bank created an extensive induction programme for all employees based not on procedures and processes, but on values. "Every single person goes on it and it's actually not about banks, it's about values. It's about the cause and it's about what we're setting out to do, that's really important." Another holds two-day inductions for all staff, including senior management. "They don't get into anything about the nuts and bolts of the jobs they're going to do. Whether you're joining as a senior person or as a junior person you always spend your first two days reflecting on what our culture is."

### What has worked and what has not?

These institutions tend to find that initiatives that embrace their size are the most effective. “I think we’re so lucky because we’re so small. 3,000 people – you can get them all in one room if you want to. So it means as a leadership team we can get our arms around the entire business.”

Diversity, too, is a stronger theme in this category, more egalitarian institutions. As one senior executive comments, “It’s probably not a coincidence that our CEO is a woman and there are four of us on the executive team who are female, so four of our nine, so I do think in terms of running a balanced bank that that is an important component of the recipe.”

What has not worked so well, for these institutions, is when they have tried too hard to talk about, rather than demonstrate, their cultural difference. In the words of one executive, “Anything where it’s not seen to be followed through, anything that’s said for the benefit of the media and is not authentic.”

Similarly, some of the challenger banks struggle with the logistics of giving every employee a voice. For example, one bank describes

how “People are always coming up with lots of ideas and we encourage people to write to the CEO and they do. We’re small enough to be able to have a dialogue.” This bank did not consider this a problem now, but it would potentially get more challenging as it grows.

### What progress has been achieved?

As with the banks which were less, or not, affected by the financial crisis, the challenger banks did not feel the need to prove that their culture had changed. They were, however, keen to point to proof that their culture continued to be an effective measure of competitive advantage and commercial success.

### What challenges have been encountered?

The challenges for these institutions tend to be those that any smaller, more devolved organisation would struggle with, in terms of ensuring consistency of message and adoption within a culture of individual opinion and responsibility. As one executive says, “In a dispersed organisation it’s difficult, that’s the hardest thing. In terms of trying to define the values in the organisation, that’s relatively

straightforward. Trying to make sure that they’re lived, day in, day out and not just face to face, but they’re manifested in our online presence as well.”

“ For us, it’s when the brand, when we are recognised as a different sort of bank in terms of our values, our approach to banking. For the economics that means we have a lower customer acquisition cost and a lower retention cost than our competitive banks do. ”

The other key challenge is that of retaining their cultural and competitive edge, as the rest of the banking industry embraces culture. As one says, “I guess the cultural challenge is not ever getting complacent and to constantly reinvent ourselves, because we’re operating in a fast-moving world and we want to continue to be the leading challenger bank, and to continue to be the leading challenger bank, we mustn’t allow ourselves to get into a comfort zone.”

“ The larger challengers with a legacy heritage have to contend with past cultures, which can be difficult (though not impossible) to change. They have perhaps less of an advantage here, although a smaller scale always makes culture change more achievable. ”

**Warren Mead**, Head of Challenger Banks, KPMG



# About the survey

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## Basic research concepts

To undertake in-depth interviews with a broad range of senior banking executives, for greater understanding of the importance and details surrounding the subject of culture and ethical standards.

## Fieldwork details

In-depth qualitative interviews with 21 chief executive officers, heads of country operations and senior banking executives. Additional contributors included senior management, corporate compliance and cultural directors.

## Types of banking institutions

Interviewees included custodial, wholesale, retail and private banking services, as well as UK-domiciled and non-domiciled banks.

All banks and their representatives interviewed were governed and regulated under the UK financial services supervisory regime.

## Fieldwork methodology

The interviews, facilitated by the BBA, were conducted using a mixture of in-person (7) and telephone (14) interviews.

## Fieldwork dates

Interviews took place from Friday 17 April 2015 to Wednesday 20 May 2015.

At no point during the discussions did we define what was meant by culture and ethics; preferring to allow the interviewees to define their own understanding.

## Interviewees' attitudes

- All believed that it was right to explore the vitally important role of ethics and culture in banking.
- Some demonstrated sensitivity around the subject and were keen to provide absolute clarity in the information and the opinion they provided.
- Others had what could be described as reconciled acceptance to the subject, due to the high profile of cultural issues within the organisation or their own role.

## Interviewer details

The interviews and report were completed by a senior independent researcher with 20 years' experience of undertaking financial services research.





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The voice of banking

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