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SWP 28/93 THE CHANGING STRUCTURE AND ROLE OF BUILDING SOCIETIES IN THE UK FINANCIAL SERVICES SECTOR

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*(Chapter in **Management in the Service Sector**, edited by Colin Armistead, Kogan Page Cranfield Management Research Series, forthcoming 1993)*

ISBN 1 85905 033 6

1. INTRODUCTION

During the past decade, the UK financial services sector has been subjected to an unprecedented scale of deregulation. As a consequence, banks and building societies have attacked each others traditional business sectors as they have sought to take advantage of new-found freedoms. Consequently, banks and building societies are now direct competitors across a wide range of financial products and services with banks competing aggressively for the traditional core mortgage and retail savings markets of building societies while the societies now have the powers to provide, for example, an extensive range of money transmission services which had previously been monopolised by the commercial banks. Adjustment to this new environment has been a daunting challenge for the societies but, based on the evidence so far, they have demonstrated that they are capable of making the necessary transformation. This paper examines the challenge of change facing the societies, drawing on the experience of the past few years. In particular, it focuses on:

- the nature of the new environment and the opportunities it offers for new business activities

- the changing structure of the building society industry as merger activity accelerates in the new environment

- the challenge of change at the building society branch level

The future for the societies is highly complex and, despite their success to date, they will still face considerable challenges in the years ahead both nationally and, increasingly, internationally as the Single Market in Europe develops. The purpose of the analysis reported in this chapter is to create a platform for continued debate amongst the societies in terms of future strategies concerning their changing objectives, merger activity, branch networks, new product development, diversification and marketing.

2. THE ORIGINS AND GROWTH OF THE BUILDING SOCIETY MOVEMENT

The foundations of the UK building society movement, with its status of mutuality, were laid in the late 18th century when groups of people banded together to build houses. The group members would pay a weekly contribution to a fund which was used to buy land and then to finance the building of houses. When all the members had been housed the society was disbanded. By the middle of the 19th century, societies had largely ceased to build homes but were changing to become permanent institutions which supplemented their funds by borrowing from people who did not want to buy houses and lending to other people who wished to buy existing dwellings or to finance the building of new properties.

Building societies operate under their own specific legislation, rather than the more general company or banking laws in the UK. The first Building Society Act was passed in 1874, establishing the societies at that time as a distinct legal form operating under specific, though restricted, objectives. There were three additional Building Society Acts in 1884, 1939 and 1960 and a further Act in 1962 which was mainly a consolidating statute. There was thereafter no major legislative change to affect the method of operation of building societies until the implementation of a new Act in 1986 (see Section 3 below).

In the years since its origin, the building society movement has been transformed from a very large number of small, individual societies, to a smaller number of larger societies with branches which in many cases are spread right across the country. Although the number of societies has decreased year by year, the number of members - investors and borrowers - has dramatically increased, particularly during the post-war years. The building societies have established themselves as major specialised financial institutions in the UK for personal sector savings and have consistently been the principle providers of finance for private sector house purchase. As shown in Figure 1 below, the number of societies still in operation at the end of 1992 was 105. It can be seen from the figure that by the end of 1992 the number of building societies had fallen to just over 4% of the number in existence at the start of this century. Table 1 shows how this rate of decline has varied decade by decade. Between 1900 and 1930 the decline in the number of societies was fairly steady while between 1930 and 1960 the rate of decline fell. However, between 1960 and 1990 there was a sharp increase in the rate of decline with the 1980-90 decade showing the peak at an annual rate of decline of over 8%. This was a decade of extensive deregulation in the financial services sector (see below).

INSERT FIGURE 1

INSERT TABLE 1

The decline in the number of societies has been accompanied, not surprisingly, by an increasing share of the building society assets being accounted for by the larger societies.[1] Table 2 below shows trends in the degree of concentration of the building society industry over the period 1930-1991. It will be seen that the largest five societies gradually increased their share of total assets until 1988, though since then this share has declined by almost 2% (partly because the

1. For further details see Coles (1992).

former Abbey National Building Society converted to plc status in 1989)[2]. The share of the next group of five societies grew steadily until 1985, falling away in the late 1980s but has since grown again. Overall, the share of the largest twenty societies has grown steadily year by year, from 65% in 1930 to 92.5% by the end of 1991. In total, the number of borrowers in the UK today with building society mortgages is now in excess of seven million (in 1970, the number was less than four million).

INSERT TABLE 2

3. DEREGULATION IN THE UK FINANCIAL SERVICES SECTOR

Since the arrival of a Conservative government in 1979, the UK financial services sector has been subjected to an unprecedented scale of deregulation. Relaxation of interventionist policies which had dominated business during the preceding decade began with the abolition of foreign exchange controls, followed by the removal of restrictions on domestic bank lending (via the ending of the Supplementary Special Deposits Scheme - so called "the corset"). This relaxation on lending by the commercial banks was the signal that the banking community had been waiting for to move into new areas of business activity, especially the then lucrative UK mortgage market (which had previously been dominated by the building society movement through an effective cartel arrangement). In 1981, the authorities also relaxed their controls on interest rates by ending the formal announcement of the Minimum Lending Rate as well as the abolition of a reserve asset ratio requirement on banks' balance sheets.

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2. It should also be noted that there was a particularly sharp jump in the market share of the top five societies following the merger of the Nationwide and Anglia Building Societies in 1987.

These changes were in parallel with the ending of the Building Societies Association (BSA) mortgage rate cartel, followed by further relaxation of controls over building societies in 1983 which opened up access to wholesale funds and the sterling Eurobond market. The effect was to increase competitive pressures still further in the financial services sector by giving the societies access to a cheaper source of funds compared with their traditional (though still dominant) source of retail deposit-taking via the branch networks. At the same time, the commercial banks saw a gradual reduction in the legal requirements for their cash deposit ratios (from 1.5% in 1981 to 0.4% by 1991). The Financial Services Act (1986), the Building Societies Act (1986) and the new Banking Act (1987) gave still more momentum to the process of liberalisation in the UK financial services sector.[3]

Table 3 below provides a summary of the key UK financial deregulation measures and their timing over the period from 1979 to date. These measures have also coincided with other factors beyond regulatory developments, particularly the internationalization of financial markets and the development of information technology, all of which have contributed to a dramatic increase in competitive pressures both in the UK and overseas.

INSERT TABLE 3

The effect of deregulation and increased competition has meant that during the 1980s the UK financial services industry (including business services such as those relating to investment advice) achieved the highest rate of growth compared with any other sector of the economy in terms of output. According to official statistics, the real output of financial services doubled during the period

3. For further details see Johnson (1991) and Ennew et al (1990).

1979-1989 (with an average annual growth rate of over 7%), while real output for the economy as a whole rose by one quarter. During the same period, the average annual rise in employment in the financial services sector was just over 5% with a roughly 2% increment in labour productivity.

Apart from the impact of deregulation, this impressive performance of the financial services sector can also be attributed to a general rise in living standards during the 1980s. As the general level of economic welfare has increased, so the consumption of financial services has tended to increase also but at an even faster rate. This phenomenon is not new, nor is it unique to the UK, and highlights the fact that as consumers become wealthier so they tend to save and borrow more and generally become more sophisticated as consumers of financial products. Consequently, the effect of this has been that the scale and range of financial investments on offer have become greater with a co-incident expansion in the provision of business-related services concerning, for example, legal advice about investment and house purchase. This is reflected in the marked increase in owner-occupation and the wider share ownership in the UK during the 1980s.

An important consequence of the deregulatory measures shown in Table 3 above is that banks, building societies and other financial institutions are now in direct competition across a wide range of financial services and products. For example, banks now compete aggressively for the traditional core mortgage business of building societies, while the societies have exploited their new freedom to provide an extensive range of money transmission services, many of which were previously exclusive to the commercial banking sector. In general, competition across the various types of institutions has focused on five key areas of business activity. These areas and the key players involved are listed below.

Business Activity	*Key Players*
Mortgages	Banks, building societies, insurance companies and specialist suppliers such as the centralised lenders
Money Transmission Services	Banks and building societies
Higher Interest Accounts	Banks and building societies
Longer Term Investments	Insurance companies, unit trusts, stock brokers (and, more recently, some of the major building societies)
Attraction of Young Investors	Banks and building societies

It is against this background of deregulation and the increased competitive environment that we shall examine the changing role and structure of the building society movement in the UK and, specifically, explore the ways in which these developments have affected operations at the branch level. First, however, we set the scene by analysing in some detail the nature of the new environment in which the societies find themselves, setting out the extent to which they now have greater freedom to expand their activities.

4. THE NEW ENVIRONMENT OF BUILDING SOCIETIES

On 1 January 1987 the UK building society industry was presented with a new regulatory framework enshrined within the Building Societies Act (1986). As noted above, the building societies had previously been facing increasing competitive pressures from other financial institutions, primarily the High Street banks and new players in the mortgage market (namely centralised lenders). The removal of artificial controls from their balance sheets by 1980 gave commercial banks the freedom they needed to compete for both savings and mortgage business. At the same time, technological developments throughout the 1980s increasingly broke down competitive barriers between financial institutions generally and the building societies quickly found themselves coming under increasing pressures as they struggled to match their competitors' services.

As a consequence, building societies began to experience significant encroachment on their traditional business, namely mortgage lending for house purchase. In particular, the banks became the predominant providers of mortgage finance at the more expensive end of the UK housing market which gave them an opportunity to cross-sell other high value-added products (such as house insurance and personal pensions). In 1980, bank mortgage lending totalled £600 million, but had risen to £5,000 million by 1982. In market share terms, this represented a change from 8% to 36% of new lending in just three years. This success had largely been achieved by offering discounts on the standard mortgage rate for larger loans. The societies, through necessity rather than choice, were forced to examine their mortgage lending procedures and terms so that many reacted by shifting their lending-down market. The effect, however, was a general lowering of the quality of their mortgage business compared to that which had prevailed in the past. Many societies also reacted by abolishing the practice of charging higher interest rates for larger loans.

In just a few years, therefore, the building societies moved from an environment in which they faced little competition to one in which competitive pressures were rapidly intensifying on both sides of their balance sheets (the savings side was also being encroached from the early 1980s as a direct result of the government's decision to fund a larger share of its budget deficit through a range of tax-free and/or index linked financial instruments such as National Savings). Retaliatory measures by the societies were, however, limited because of the restrictions at that time enshrined within their legal framework which generally prevented societies from substantially altering the pattern of their business activities.

It is not surprising, therefore, that the pressure for change in their regulatory framework to allow greater freedom for activity, came from the building societies themselves. It is fortunate that this pressure for change happened to coincide with the then government's own objectives of deregulation and competition, particularly in the case of the financial services sector. At the centre of the new legal framework surrounding building societies lie the capital adequacy rules enshrined in the 1986 Building Societies Act. Essentially, these rules provide a more sophisticated system for measuring the capital adequacy of building societies and also bring the prudential requirements for their operations more into line with those which apply to commercial banks. The societies are compelled to comply with these rules in order to be able to take advantage of new areas of business. The most important consequence of the implementation of these capital adequacy rules is that the societies now have become increasingly conscious of the need for greater profitability. Meeting traditional reserve and liquidity requirements is no longer sufficient since higher profitability in their activities not only ensures the maintenance of adequate capital reserves but also provides societies with the opportunity to take advantage of the new regulations which permit them to expand their business activities. In particular, Schedule 8 of the 1986 Act (as well as amendments to the Schedule implemented by the government in August 1988) gives societies the power to operate in the following new areas [4]:

4. Full details are given in BSA (1988) and Nellis and Litt (1990).

- Money transmission services
- Foreign exchange services
- Making or receiving payments as agents
- Management, as agents, of mortgage investments
- Provision of services relating to the acquisition or disposal of investments
- Establishment and management of personal equity plans
- Arranging for the provision of credit to individuals and unincorporated businesses
- Administration of pension schemes
- Arranging for the provision of insurance of any description, including life insurance
- The power to establish or take over existing estate agencies
- The power to undertake fund management, including offering their own unit trusts

Thus, from January 1987 building societies in the UK have had the power not only to offer a full range of money transmission services with cheque books, cheque guarantee cards, overdraft and foreign exchange facilities but also to conduct business across a wide range of other activities that hitherto had been monopolised primarily by banks, insurance companies, fund managers, etc. In many cases, full service cheque book accounts are available with interest paid on credit balances with the consequence that all of the large banks have been forced to offer similar accounts. Inevitably, this has put pressure on margins and has focused attention on profitability and performance. This greater consciousness of profit, however, has opened up many related, and in some cases, sensitive issues. Staff performance and appraisal now receive much greater attention with appropriate reward systems high on staff development agendas. In addition, the societies (as well as banks) face an even more fundamental question: how can profitability be measured accurately? The societies have been accustomed to the concepts of "adequate" reserves and liquidity but now questions are being asked concerning the difference in profit margins on different products, such as on a mortgage versus that for a particular type of savings account. Furthermore, profitability as a target and key performance measure highlights the problems associated with making comparisons between branches in different locations, facing very different competitive environments. Such questions have acted as the catalyst for driving change within the building society industry. The effect has been a dramatic cultural transformation within building societies generally both in terms of staff attitudes, management practices and business expectations (discussed further in Section 5).

While new strategies within a new business environment are being formulated at head offices, implementation is ultimately the responsibility of branch managers who, in general, are required to perform without the complete information which they consider necessary for them to be fully effective[5] Thus, perhaps the greatest challenge facing building societies today relates to the development of new policies which address the strategic importance of the role of the branch managers and, ultimately, the branch network.

As the speed of merger activity between building societies has increased in recent years, so branch rationalisation has become a major feature of current business strategies. This rationalisation is not unique to the building society sector - banks in general have seen a reduction in the total number of their branches year by year during the past decade. Table 4 below shows the pace of the branch rationalisation programme being carried out by building societies and

5. For further details of how corporate strategies are changing in response to the new challenges see Balmer and Wilkinson (1991).

banks in recent years. It will be noted that, apart from 1989 when the banks' figures first included the branches of Abbey National, there has been a steady decline in the bank branch network throughout the whole period. This decline was especially marked during 1991 when there was nearly an 18% fall in the number of bank branches, reflecting the weak financial position of almost all banks in the UK in the wake of an unprecedented scale of business bankruptcies and personal sector debt problems as the economic recession deepened. In contrast, the number of building society branches increased steadily from 1980 up to and including 1987. The fall of nearly 10% in 1989 was largely due to the exclusion in that year of Abbey National branches. It is notable, however, that branch rationalisation in the building society sector has continued since then up to the end of 1991 (latest figures available). This raises the question as to whether or not this rationalisation will continue still further in the 1990s.[6]

INSERT TABLE 4

In Section 6 below we return to the issue of branch management and the impact of the new business environment on the various aspects of branch activity. First, however, we examine more closely the cultural transformation (noted above) that has been achieved within the building society movement. This provides a useful overview of the extent and impact of the challenges of change which are being faced at the branch level.

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6. For further analysis of the prospects for branch rationalisation see Fleming and Nellis (1992).

5. CULTURAL SHIFTS IN THE BUILDING SOCIETY INDUSTRY

In the new environment of competition described above, the need for change within the building society movement across all aspects of business has never been more daunting. The greatest challenge facing the societies, apart from the necessity to change their physical operational structures in terms of management, branch networks, products etc, is the need to reassess their very culture. Coming from a "safe" background in which the speed of change was barely perceptible, the societies now find themselves thrust into an altogether more dynamic environment with competitive pressures increasing day by day. These pressures are consequently forcing management to react speedily in their attempt to bring about a change in attitude amongst staff from an emphasis on social aspects (which dominated business objectives in the past) to the hard cold commercialism which is now the dominant feature of their business environment today. For many staff, particularly those appointed prior to the mid-1980s, the transformation demanded of them must, in the words of Tom Peters, present an impression of the "world turned upside down" with even the sacred status of "mutuality" now being questioned following Abbey National's successful conversion to plc status in 1989.

In their efforts to adjust to this new business climate, the societies are demanding greater inventiveness and creative thinking of all staff. The management of head office functions, regional operations and branch performance now requires a range of skills and entrepreneurial attitudes that, in the past has not been needed.

Branch managers probably face the greatest challenge in the new environment. In the past, they have largely performed an administrative role without the necessity to be proactive in attracting new customers. Business was essentially driven by the financial criteria dictated by regional and head offices. Since the late 1980s, however, the branch managers have been urged to adopt the role of business developer, with a keener eye for new avenues of business growth and profitability. The reality now is that managers are expected to "sell", rather than sit back, as in the past, and wait for business to "walk in through the front door". This expectation has, inevitably, heightened the importance of staff training and development which is appropriate to the transformation in culture required within the branches themselves.

The concept of "planning" has also been catapulted into the building society world. Traditionally, the societies have tended to adopt a short-term stance with regard to business planning. This primarily centred on the maintenance of the flow of investment funds to service their mortgage lending. Now, in the new climate, greater emphasis is being placed on long-term planning backed up by acute awareness of a host of relevant factors, - such as demographic changes and the opportunities that these provide for new areas of business. As the UK reaches saturation point with regard to expansion of home ownership, the societies will face even greater competition for market share in the mortgage market. Customer loyalty will be of paramount importance. It is expected that, as a result of these pressures for change, some societies will follow the Abbey National lead along the plc path. Most societies, however, are expected to remain mutual but, as we noted above, they will need to achieve a balance between the maintenance of this position and a necessary degree of commercialism in their new environment.

Table 5 below provides a diagnostic checklist of many of the aspects of management within the building society industry which are undergoing a transformation from the "old" culture to a "new" culture. The former was appropriate to the sort of stable, controlled environment prior to the 1980s while the latter is appropriate to the dynamic, competitive environment of the 1990s. The "winners" will be those organisations that can successfully complete the transformation and adjust to the "new" rules.

INSERT TABLE 5

6. THE IMPACT OF CHANGE ON BUILDING SOCIETY BRANCHES

So far in this chapter we have largely focused on the impact of deregulation in terms of the general business environment of building societies. However, as noted earlier, challenge of change is probably greatest at the branch level and it is to this aspect of business activity that we now turn and report on the findings of a research project sponsored by the Cranfield School of Management involving a detailed questionnaire survey of almost 500 building society branch managers[7]. The research focuses on a number of aspects of branch activity which embrace the major challenges for building societies in the 1990s. These include the following:

- The recruitment and retention of branch staff
- Staff training and development
- Salary and status of branch managers
- The changing role of building societies
- The authority and responsibility of branch managers
- The measurement of branch performance

We summarise the findings of the research under each of the above headings.

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7. Full details of the research project and fundings are given in Nellis and Litt (1990).

6.1 The recruitment and retention of branch staff

From the questionnaire responses, there is clear evidence that since the introduction of the Building Societies Act (1986) many branch managers have been experiencing severe difficulties with regard to the recruitment of new staff, particularly cashiers and clerks (and, hence, there has been a sharp increase in the number of part-time staff). It is reported that these difficulties are particularly acute in areas in the south of the country as well as in the more affluent localities. Given these problems, the question of competitive rates of pay will have to be addressed by the societies. It was the opinion expressed by many branch managers that building society rates of pay are low compared with those of other financial institutions and that this is the principal reason for their inability to attract and retain high quality staff. In addition, many branch managers expressed the view that they would welcome the authority to determine their staff salaries with greater flexibility in order to be able to match local salary levels.

Many societies, especially the largest ones, have had a graduate recruitment policy for some years and among the medium sized societies it seems to be a policy that is gaining ground. As the number of graduates increases, the question of resistance on the part of existing staff whose opportunities for promotion may be reduced will clearly be a delicate matter for the societies to manage, particularly with regard to staff morale. A further potential problem is that as these graduates and the skills they acquire become more and more marketable in the changing financial climate, they will need to be offered greater incentives by the societies to retain their expertise.

The suggestion that loyalty to the society will no longer be a quality that is encouraged among building society staff adds another dimension to the problem of staff retention (see Table 5 above). It raises the question of the loss of investment - in terms of both time and money - in training up good staff when they depart for more lucrative opportunities.

Branch managers have also expressed strong support for the introduction of early retirement schemes within the societies and, indeed, there is also likely to be a large take-up if these are offered widely. The feedback from branch managers suggests, perhaps, that some of the older branch managers may be "finding the going tough". Their jobs have changed almost beyond recognition from what they were in the 1960s and 1970s. While many societies may be tempted to implement more attractive early retirement schemes, they must be wary of the significant loss in experience and skills that would result. A more selective policy of staff rationalisation may be preferable.

6.2 Staff training and development

Today, training within building societies is much more than being simply product knowledge based. The pressures to sell financial services are now at the top of the agenda but it is a fact that the vast majority of branch staff have few, if any, qualifications in this area. As staff experience more and more pressure from senior managers to sell, greater emphasis must be placed on the need for appropriate training. This is an issue which stands out clearly in the responses to the questionnaire survey and seems to be one of the greatest challenges facing branches at present.

Very often, the responsibility for branch training is laid at the doorstep of the branch manager. While managers generally accept this responsibility, they believe that they themselves should be trained to train - this is a view favoured particularly by the managers from the smaller societies. Looking to the future, questions will be raised as to whether or not branch managers will have the time to carry out staff training as the pressure to sell increases. On the whole, more than half of the managers in the survey expressed satisfaction with their own branch training activities - this is perhaps not surprising - as well as those carried out by head offices. Despite these views, a great majority of respondents complained about the lack of time available for training purposes as a result of other pressures, while at the same time recognising that the amount of time has increased.

Since the introduction of the Building Societies Act (1986), greater emphasis seems to have been placed on self-training and audio-visual and computerised teaching, especially within the larger societies. These developments are to be welcomed but they should not to be seen as representing a comprehensive training package. They cannot bring about the major cultural shift that is urgently required within the societies since, by and large, they tend to provide skills training only.

6.3 Salary and status of branch managers

From the responses received in the survey, it is clear that building societies are heading towards what may be a crisis with regard to motivation of branch managers. It was the unanimous opinion of respondents that the salary levels of branch managers are not competitive with those of other similar professionals and are not commensurate with their perceived status. It should be stressed here that no information has been obtained about the actual salary levels across the professions in question - bank managers, solicitors, stockbrokers, insurance agents, mortgage consultants, estate agents and accountants. Branch managers were only asked for their perceptions of how salary and status compared with those of other equivalent professionals. Building societies, therefore, face a major challenge in the future - to be faced sooner rather than later - with regard to these issues and how branch managers are provided with the appropriate incentives, given the pressures which they face at the sharp end of the business.

6.4 The changing role of building societies

Another dominant theme in the research responses involves the question of whether or not building society branch managers feel that they can compete effectively in the new environment. In this respect it is notable that a large majority of respondents expressed confidence that their societies will be able to compete. Emphasis was placed on the fact that societies come from a background in which they have a good reputation, a large customer base and considerable customer loyalty. However, it was recognised that this loyalty will come under severe strain as competitors seek to attract customers away.

Some concern was expressed by branch managers that as their societies strive to provide a full range of financial products and services, there is the danger of becoming a "Jack-of-all-trades". This again has implications for staffing levels within societies and at the same time highlights the need for specialists to cope with the more complex areas of business. This need for specialists is all the more important given the legal regulations under which financial institutions now operate. At the moment, few societies have ventured seriously into the new areas of business such as stockbroking, executorship and trusteeship. By and large, the focus is still on the relatively traditional areas, though there have been major inroads in the last few years into the personal loans market. Land services - estate agencies - have been prominent among the larger societies for several years now.

A majority of branch managers have expressed support for a strategic move by the societies into these new business areas, though not necessarily as a substitute for their traditional business. Not surprisingly, perhaps, this support is strongest in the largest and medium-sized societies where the ability to diversify is greatest though, within the present legal framework, they are limited in the extent to which they can move away from the traditional business (ie mortgages).

From the survey it appears that branch managers from those societies which have clearly identified specific strategies are those who are most optimistic about the future and the challenges which they face. This observation has very clear implications for societies in general - it is important that clear objectives are identified and that they are communicated to all staff. This is not only important for staff morale but also for planning purposes.

There appears to be only limited support for a move towards plc status - along the route recently taken by the Abbey National in 1989. While opinion is split fairly evenly among the large societies, the supporters are in the minority among managers from the smaller-sized societies. There are fears, too, of damaging the "caring image" which has developed under mutuality if the plc route is chosen. As noted before, a large majority of branch managers are confident that, as mutual societies, they can meet the challenges of the future effectively, given the opportunities to manage.

6.5 The authority and responsibility of branch managers

The survey results indicate strongly that branch managers regard their own efforts as being the most important factor in attracting business into the branches and they expect their role in this context to increase in the future. The importance of estate agents' and solicitors' referrals in providing new mortgage business is expected to decline, while the importance of branch promotions and referrals by local firms is expected to increase. The implication of these trends, therefore, is that branch managers expect to have a greater role to play in business development based on a more proactive approach. At the same time, branch managers expect the reputation of the society to play an increasingly important part in generating business.

Another recurrent view of branch managers is that they should be given more direct managerial responsibility. They expect that their role as decision makers, motivators and salesmen will far outweigh their declining role as administrators and that their involvement as personnel managers will increase. There are indications that there has been an increase in the extent to which authority is being delegated within branches. This is a trend that is likely to continue with the expansion in services, particularly if training programmes are intensified.

There are no false illusions among the branch management as to the pressures which they face and which are likely to increase. These pressures are coming from the greater diversity of operations, greater competition, the requirement for better performance, greater responsibility, as well as the legal regulations under which they have to operate. Acknowledgement is given of the fact that branch managers have been granted some flexibility in the matter of mortgage limits that they can sanction and this move is welcomed. However, demand appears to be growing for improvements in a number of other areas, particularly with regard to head office support services. Much criticism has been made of head office communications with the branches both in connection with the launching of new products and with respect to day-to-day problem solving. There is a widespread impression that head offices are not in tune with branch needs and that a greater awareness of the branch environment would be beneficial.

6.5 The measurement of branch performance

Major changes are taking place in the relative importance of the different indicators that are used to measure building society branch performance. The main traditional indicators are the number and value of investment balances and the value of mortgage lending. These are rapidly being overtaken by the profit and loss account. The survey responses confirm that the number and value of accounts is becoming less important as a measure of performance though the value of mortgage lending is expected to remain high on the rankings. In addition, the importance of commission income is expected to increase significantly and to become one of the principal indicators of branch performance.

Particular problems arise for building societies in making comparisons of performance between branches that have particular local circumstances which impinge upon their businesses. It makes no sense to expect one branch located in an area largely populated by young couples to have similar targets to another branch located in an area largely populated by retired people. The bottom line - that is, profits - may turn out to be very different in each case, largely due to the fact they have different customer bases. The whole question of branch performance is one that must receive immediate attention within building societies given the greater consciousness of profitability itself. The pressures which the societies face are likely to decrease the significance given to performance based on "numbers" of accounts - greater emphasis is likely to be placed on values such as total lending and deposits and so-called "key customer accounts".

7. CONCLUSIONS

In this chapter we have described the changes that have taken place in recent years in the nature of the business environment within which building societies operate. The deregulation of the 1980s has been unprecedented in the history of the building society movement and with the creation of the European Single Market at the start of 1993, it is likely that the pace of change will be unrelenting in the 1990s and beyond. It is inevitable that there will be further major changes in the structure of the UK and European financial services sector in the coming years. The societies, which will not be exempt from these changes, will be forced to trim their management expenses and develop effective branch management systems as the culture of the organisations moves further away from that based on mutuality to one which is focused on the achievement of a sustainable competitive edge and an adequate level of profitability.

Particular attention has been given in this chapter to the challenges faced by staff and managers operating at the branch level. The analysis presented is based on the research findings from a detailed questionnaire reported in Nellis and Litt (1990). In general, it is found that branch managers look to the future with some excitement and recognise the challenges afforded by the wider range of financial products and services available to them - particularly among the larger societies. They recognise the opportunity to increase profits but appreciate the need to be ever conscious of the need to improve the quality of the services that they offer. In contrast, there are no false illusions about the pressures created by the increase in competition and the pace of change within the building society movement. Further aspects of the survey results suggest that, at the personal level, branch managers perceive themselves having strengths in a number of areas. The experience they have already accumulated in traditional building society business is seen as their main strength but they are fully aware that they lack specialist knowledge in the new areas of business though in these rapidly changing circumstances qualities of flexibility, adaptability, drive and commitment are seen by many managers as their principal strengths.

Most managers welcome the opportunity to enhance their own performance and skills through their involvement with new products and services. They also recognise the opportunity thus presented to enjoy a more varied career with potential rewards in the form of higher salaries and increased promotion prospects. On the other hand, there is anxiety that failure to achieve targets could threaten these promotion prospects. The threat of merger or takeover also clouds the horizons of a number of managers such that the challenges of the future, therefore, may result in less loyalty as well as less job satisfaction.

In conclusion, the evidence of the past few years suggests that, despite the enormity of the challenges which they have faced and will continue to face, building societies will remain as a dominant force in the UK financial services sector for many years to come. They have demonstrated that they have the ability and confidence to compete in an aggressively competitive environment despite the speed of transformation required of them in terms of business operation and culture. They have also demonstrated the essential benefit of their new regulatory framework to the public via a dramatic extension in the range of choice in the provision of financial services. In addition, experience so far suggests that the Building Societies Act (1986) has also contributed significantly to an increase in the standards and reduction in costs of all parts of the market for personal financial services in the UK. That they have not only survived but have actually embraced the new environment positively through successful diversification demonstrates the inherent strengths of building societies to cope with the challenges of change and to adopt the appropriate role for the future.

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TABLE 1 SUMMARY OF UK FINANCIAL DEREGULATION MEASURES 1979-1991

Year	Deregulatory Measures
1979	■ Abolition of foreign exchange controls
	■ Relaxation of government controls over BSA mortgage rates
1980	■ Abolition of Supplementary Special Deposits Scheme (the 'Corset')
	■ Abolition of formal announcement of Minimum Lending Rate
	■ Abolition of banks' reserve asset ratio
	■ Reductions in banks' cash ratio (from 1.5% to 0.5%)
	■ Greater freedom for building societies to compete for retail deposits
	■ Ending of BSA mortgage rate cartel
1982	■ Abolition of remaining hire purchase controls
1983	■ Further relaxation of controls over building societies (opening up access to wholesale funds and the sterling Eurobond market)
	■ Banks' cash ratio reduced further to 0.45%
1987	■ Financial Services Act (1986)
	■ Building Societies Act (1986)
	■ Banking Act (1987)
1988	■ Further relaxation of controls over building societies in terms of access to wholesale funds, the issue of subordinated debt and the provision of banking, investment and insurance services
1989	■ Banks and building societies permitted to issue sterling commercial paper
	■ Abbey National Building Society converts to plc status
	■ Building societies allowed to provide a wider range of money transmission services
1991	■ Banks' cash ratio reduced to 0.4%
	■ Building societies permitted to issue permanent interest-bearing shares

Source: HM Treasury (1991)

TABLE 2: RATE OF DECLINE IN NUMBER OF BUILDING SOCIETIES 1990-1992

Decade	Annual Rate of Decline %	Decade	Annual Rate of Decline %
1900-10	2.8	1950-60	1.2
1910-20	3.0	1960-70	4.0
1920-30	2.1	1970-80	5.5
1930-40	0.7	1980-90	8.1
1940-50	1.5	1990-92	5.3

Source: Coles (1992), p 6

TABLE 3: THE GROWTH OF CONCENTRATION IN THE BUILDING SOCIETY INDUSTRY BASED ON SHARE OF TOTAL ASSETS

Year	Largest 5 Share of Total %	Next 5 Share of Total %	Largest 10 Share of Total %	Largest 20 Share of Total %	All Societies Total Asssets £m
1930	39.1	14.4	53.4	65.0	371
1940	38.0	12.3	50.3	60.7	756
1950	37.3	11.5	48.9	62.5	1,256
1960	45.3	11.6	56.9	68.6	3,166
1970	50.1	14.2	64.3	77.4	10,819
1980	55.4	15.7	71.0	84.3	53,793
1981	55.1	15.6	70.7	84.8	61,815
1982	55.7	17.3	73.0	86.3	73,033
1983	55.7	17.6	73.2	87.0	85,868
1984	56.3	17.2	73.6	87.7	102,688
1985	56.6	19.9	76.4	88.6	120,764
1986	56.9	19.8	76.7	89.2	140,603
1987	60.8	18.5	79.3	89.9	160,097
1988	62.5	18.2	80.7	90.8	188,844
1989	61.0	18.1	79.1	89.9	187,012
1990	59.9	19.8	79.7	91.2	216,848
1991	59.2	21.8	81.0	92.5	243,980

Source: *Appended version of Table 9 in Coles (1992), based on individual societies' balance sheets, either directly, or as published in the Building Societies Year Book. The figures are an aggregation of societies' financial years ending between 1 February of the year in question and 31 January of the following year.*

Note: *The Halifax Building Society makes up its balance sheet as at 31 January and the Leeds Permanent on 30 September. Until 1989 the Woolwich also had a year end of 30 September. Since 1988 Nationwide has had a year-end of 4 April. The table is not, therefore, comparing like with like, but the error is minor and thus the trends are a realistic reflection of what has been happening.*

TABLE 4: THE UK BRANCH NETWORK - BUILDING SOCIETIES & BANKS

	Building Societies[a]		Banks[b]	
	Number[c]	Annual % Change	Number	Annual % Change
1980	5,684	-	14,756	-
1981	6,162	8.4	14,738	-0.1
1982	6,480	5.2	14,669	-0.5
1983	6,643	2.5	14,487	-1.2
1984	6,816	2.6	14,359	-0.9
1985	6,926	1.6	14,294	-0.5
1986	6,954	0.4	14,013	-2.0
1987	6,962	0.1	13,828	-1.3
1988	6,912	-0.7	13,722	-0.8
1989	6,236	-9.8	14,110	2.8
1990	6,051	-3.0	13,526	-4.3
1991	5,921 [d]	-2.1	11,110	-17.9

Notes: (a) Abbey National figures are included in those for building societies only up to and including 1988; after 1988 they are included in those for banks.

(b) Girobank branches are not included in the figures.

(c) Total number of offices (including one-office societies).

(d) Provisional figures provided by the BSA.

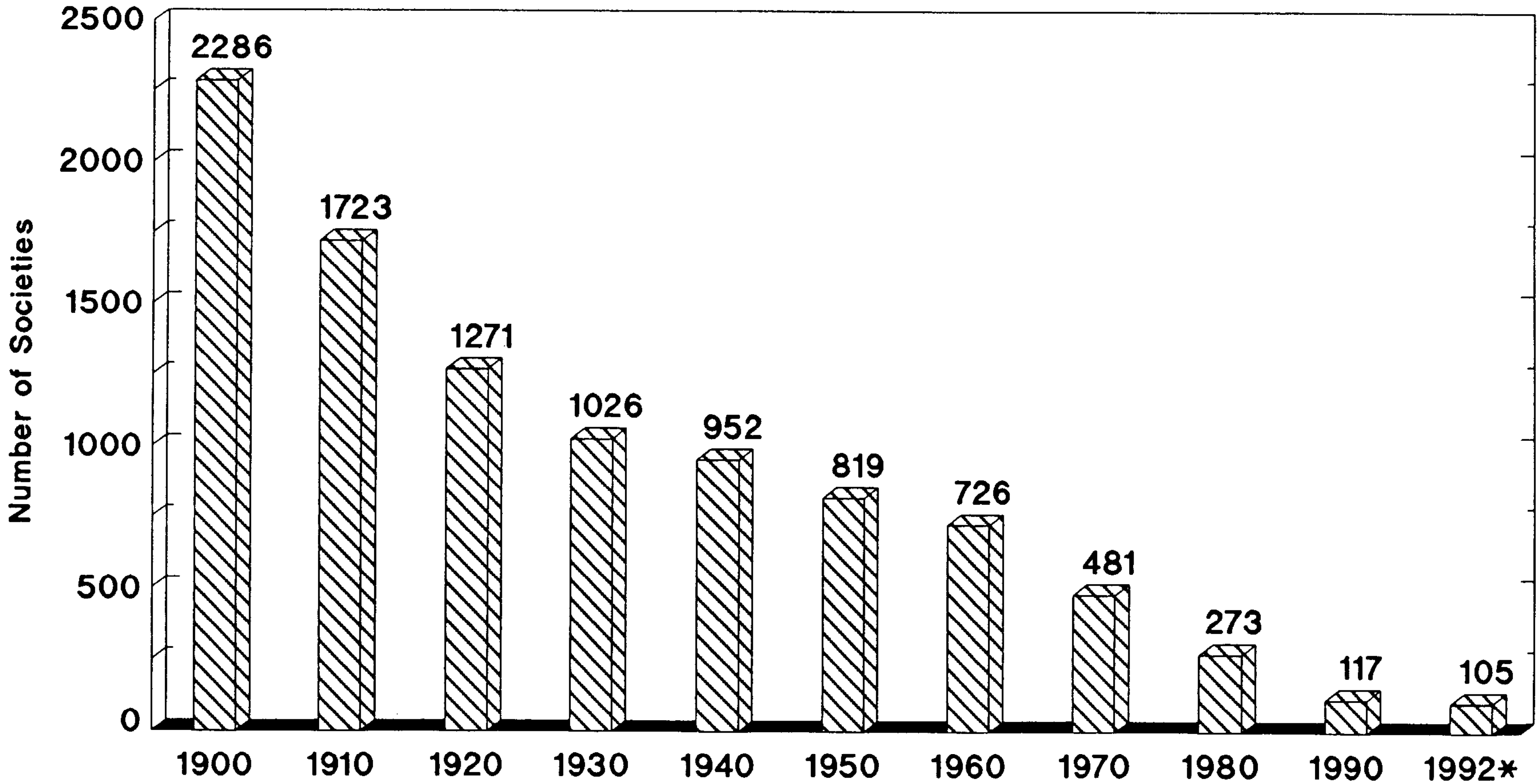
Source: *Annual Abstracts of Banking Statistics, Volumes 8 and 9, Statistical Unit, British Bankers' Association, London.*

TABLE 5: BUILDING SOCIETY MANAGEMENT STYLES, OLD AND NEW

Aspects of	'Old' culture	'New culture'
Objectives	Social	Commercial
Key tasks	Administration	Business Development
Promotion and power	Seniority, general skills and experience	Expertise, specialisation and training - more external recruitment
Structure	Centralised and bureaucratic	Decentralised and flexible
Planning	Short-term, based on tradition	Long-term, based on research
Decision making	Rules and regulations	Greater personal initiative
Relationships	Status and individual roles	Job content and teamwork
Appraisal systems	Based on effort, loyalty criticism of mistakes	Based on performance, results and praise
Staff attitudes	Loyal and proud of the society	Hopefully the same
Employment	Secure, well paid, successful and caring	Striving for achievement to ensure success, while still caring

Source: Macey and Wells (1987) Macey, R and Wells, D "New Legislation Accelerates Change in Building Society Culture." Management Accounting, *July/August 1987, pp 34-36)*

Figure 1. Number of Building Societies Great Britain, 1900 - 1992



Source : Annual Reports of the Chief Registrar of Friendly Societies and of the Building Societies Commission

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