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OPEN INNOVATION WITH CUSTOMERS IN FINANCIAL SERVICES

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Abstract: *The Dutch Financial (FS) Services industry is known for its variety and diversity in financial products and services, that have been created and developed by firms themselves. Customer involvement in the development of new products was something very unusual, because of its risk and because consumers consider financial matters as complex and not exciting at all. However, Dutch FS firms are slowly becoming aware of the potential to create new products and services with the participation of their customers, leading to products and services that are really wanted and needed by consumers. Two cases of firms that have taken this first step to involve their customers in this co-creation will be discussed.*

Key Words: ***Open Innovation, Customer Involvement, Financial Services, Netherlands***

1. INTRODUCTION

This paper deals with the reasons for a low innovativeness in Dutch Financial Services (FS) industry. It identifies the causes and discusses the open innovation prossibility for FS with their customers, based on insights developed in other industries.

To substantiate this viewpoint, two cases where customers hav been involved in the innovation process, will be presented and discussed. One case is about a mortgage bank, where consumers participated in the development and configuration of new mortgage products and services. The other one is about an insurance company that renewed it's marketing with the aid of consumers.

The paper concludes with an advise towards the Dutch Financial Services firms.

2. INNOVATIVENESS OF THE DUTCH FS

The Dutch Financial Services (FS) industry is known for its large variety and diversity in products and services. If one is looking for a way to finance a new house, people have diverse possibilities of achieving this, for instance through a mortgage, plain lending, leasing, investing in stocks, taking a life insurance, or by taking a combination of or combinations within these products, e.g. a mortgage based on investing and savings. This may indicate that the Dutch FS is highly innovative. But if one looks more closely to these products, one will discover that they are all based on or are clones of the traditional financial products, developed for P&C insurance, loans and savings. The difference lies in some exotic name, the interest rate, the currency of the product, or its purpose. Furthermore, brand difference has also vanished; consumers don't really distinguish any differences between all these financial products and become confused or mislead by product names or advisers' information. The result is that Dutch consumers have an average of four different financial service providers with which they posess, in many cases, similar products, like two bank accounts (one for daily payments and one for savings), several property insurances covering the same occurrance multiple times, and such [1]. Consumers don't feel any need to switch from provider, because they are all the same.

Over the past decade the Dutch FS have been more concerned with growing through mergers and acquisitions, and cost cutting programs, like the closing of bank branches, standardizing products and services, and striving for mass production, than in serving their customers with the tailored products and services. Compared to other industries like the chemical, and electro technical industries, innovativeness in the Dutch FS is relatively low and declining each year. Only 15% of the FS innovations are developed with or by external partners [2, 3], of which a large part by governmental legislation.

Each year Dutch corporations spend about 8 billion Euros - of which about 300 million Euros by the FS industry – on innovations. About 80% of those expenditures are spent on new products and services that the marketplace has little use for. Certainly no one consciously pursues failure but lacking refined tools to improve performance, much is wasted. In that environment the cost of getting it wrong weighs heavily on product and brand managers and marketers. It is obvious that the few new products and services that are developed in the FS industry are not what consumers really are waiting for.

3. THEORITICAL DISCUSSION

3.1. Market and customer orientation

Research shows that the success of innovations is highly dependent on the market- and customer orientation of the firm that innovates [4-8]. FS firms should therefore need to focus more on customer- and market needs to create effective innovations.

The poor results of product development and introduction have common roots in the way organizations view their customers, according to Zuboff and Maxmin [9]. During the same period that FS have been stalling in the development of customer-centered innovations, society has also been changing with a noticeable trend towards greater consumer empowerment, resulting in consumers making their own decisions on products to purchase in financial services, like insurance policies or pension plans. Zuboff and Maxmin claim that the corporate business model of mass production and mass consumption (abetted by mass media marketing) are a poor fit for a population of consumers that is richer, better educated, and more time starved than any generation in history. Today's customers are taught from an early age to think of themselves and their needs as unique and they expect tailored solutions from vendors, not mass market products [9]. The ongoing development in information technology has also accelerated this phenomenon by making information on products, costs, risks, and such more accessible for consumers.

Nevertheless, consumers don't seem to switch easily from providers because of a low involvement and high switching costs. This viewpoint is supported by academic research that has shown that the majority of individuals do not have an inherent interest or derive much pleasure from financial services [10]. There also seems to be a great loyalty with customers to financial services because of inertia, rather than any strong feelings of brand loyalty, caused by a lack of differentiation in the market [11-13]. Because of this FS firms have little incentive to encourage customer involvement [10], thereby reinforcing consumers' indifference.

3.2. Customer involvement

In the wider service literature it has been shown that increased customer involvement either during the search or at the point of purchase can reduce levels of perceived risk [14, 15] and increase levels of customers confidence when making product choices [16, 17]. Research indicates that a growing part of consumers reveal a desire to have more information about products and emphasize the need for increased involvement with financial service providers via greater deliberation and talking [10]. There is also recent research that shows that the involvement of customers in an act of co-production or co-creation, can lead to an increase in affective customer loyalty [18]. This is underlined by the Green Paper COM(2007) 226 by the EC which strives to empower consumers to make the right decisions for their financial circumstances, based on several elements, including financial literacy; clear, appropriate and timely information provision; high-quality advice; and a level playing field between products perceived as having similar characteristics. Empowered consumers may be more confident in seeking out the best deals to meet their needs, regardless of the location of the financial services provider [19]. Unless these issues are addressed, the majority of customers will continue to lack confidence when purchasing financial products [10].

Other review studies have concluded that to develop successful new products, a firm must acquire an in-depth understanding of user needs [20-22], which requires user involvement in the development process. Similarly, research has shown that user or customer involvement is an important success factor for new services as well [23, 24]. The idea of enabling customers to co-design and co-develop innovations has caught academic attention with the research of Eric von Hippel, a professor of the MIT. In the late 1970s he discovered that a large part of innovations by firms are accounted for by users and not by manufacturers solely [25, 26]. In the last decade a large amount of academic research has been executed on this subject, showing that customer involvement in new product or service development is beneficial to the success of the innovation.

4. CUSTOMER INVOLVEMENT BY DUTCH FS

4.1. Risk of fraud and attrition

Another reason for not involving customers in the deliverance, production or innovation is be that FS firms think this is too great a risk, as customers can freely access product or service data, information, and modules, enabling them to change features in a way that gives the best result, but decreasing profits for the firms, or committing fraud. There is research that argues that less direct contact between the customer and the service provider enables a greater chance for maximum efficiency [27]. Involving customers in the service process also increases workload and the chance for conflicts for service employees because of the additional uncertainty [28].

There is a part of the academic world that warns for caution on the subject of relying too much on customers in innovations [29-32]. Customers can be protective or closed concerning their inventions or innovations, or simply can't be trusted concerning their commitment to participate in the innovation process, often leading to an early withdrawal from the process [31] or a low productivity because of a lack of knowledge what to do [33]. FS firms could therefore argue that it would be better not to allow customers to co-create, in order not to make extra, unnecessary costs or risks.

Even though that there is no consensus on whether or not to involve users and consumers directly in innovations, a growing body of empirical work shows that customers are the first to develop many and perhaps most new industrial and consumer products and services [34-37]. Further, the contribution of customers is growing steadily larger as a result of continuing advances in computer and communications capabilities. And, as we have argued before, consumers are more and more demanding a vast role in the creation of goods and services. The manufacturer-centric model, which resembles the Closed Innovation model described by Chesbrough [38] is losing ground.

4.2. Growing awareness

As a result , FS firms are becoming aware of this potential role for their customers, and are willing to surpass their initial inhibitions or reluctance in involving or engaging with the customers. Evidence for this can be observed: banks are reopening the previously closed branches, insurance providers start to mass customize insurance service by providing online tools so consumers can tailor the insurance to their needs (for an example see **Error! Reference source not found.**), the two largest organizations for financial services intermediaries have announced to improve their image towards consumers by taking their needs and demands seriously [39].

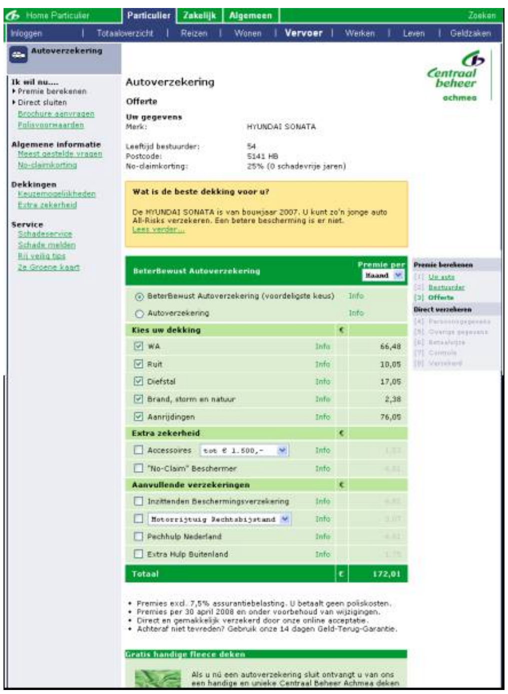

Fig. 1: *Example of a mass customized car insurance (www.centraalbeheer.nl).*

As a consultant in a firm that specializes in advising and supporting its clients in programs for obtaining customer insights, shaping customer interactions, developing new business and retaining customers, the author has lately been more and more involved in several projects in which FS firms seek to involve their customers in order to better understand their needs and to develop services that are really needed by these customers. One of the developments that indicates this is the growing demand for ZMET® researches. ZMET® stands for Zaltman Metaphor Elicitation Technique, and is a qualitative in-depth consumer research method that exposes the unconscious thoughts and feelings of participants on certain subjects [40]. The author's firm is licensed for this method and has now performed over 30 of these research projects of which about 70 percent for FS companies. But there is also a growing demand for new product or service development by these FS companies observable. Two of these projects will be presented from here on.

5. CASE STUDIES

5.1. Case study #1: new mortgage development

The first case presented in this paper is about the consumer involvement in the ideation of some new mortgage products for starters. The FS firm that is concerned in this case is a small subsidiary bank of a large insurance company in the Netherlands. The bank is mainly specialized in mortgages, but also delivers other bank services like savings, loans, etc., all except for payment accounts. The bank is only a small player in the field of mortgages with less than 5 percent market share. It is, however, known as a trustworthy money-lender, but also as very particular and conservative about its customers and financial services.

The mortgage market in the Netherlands has been booming but is reaching its limits. Booming because the prospering Dutch society leads to everyone wanting his or her own home or place to live and having the money to fulfill this dream. Reaching limits because the demand for new houses is greater than what is built every year. The effect of this latter phenomenon is that the flow of house-owners to newer and more expensive houses is stagnating, thus leaving little space for starters in the house-owning market to acquire a first and cheap house. These starters are mainly young adults that also have this dream to own their own house and are yearning to fulfill it. Because of the stagnating construction of new houses prizes for existing houses are rising every year, making it, together with the stagnating exit of former house-owners from these existing houses, the more difficult for starters to acquire their own first house at reasonable and affordable costs. Apart from the obstacles of physically acquiring a house, this group also has difficulties in getting a proper mortgage to finance the acquisition.

The goal of the project was to develop some new mortgage products for this starters group, making it easier and more comfortable for them to get a mortgage. Whereas the developing time of new products and services could take more than a year in this bank, the ambition was set to aim for a time to market of 6 months at the most. Because the bank wished to launch at least 2 or 3 new marketable mortgage services it was planned for to involve consumers in the project. This would ensure that only those ideas for which consumers saw the relevance towards their needs would be developed further on.

A project team, consisting of 3 bank employees - marketing, market intelligence and communication - and 3 consultants - of which the author was one -, was appointed to carry out the mission. The following steps and activities were executed. First the project team performed a desk research to identify the needs of starters, the context in which these needs existed, and the possible frustrations and problems these starters encountered in fulfilling their needs. This step resulted in the identification of three starter segments which make up about 75 to 80% of the total starter population, briefly described here.

One segment consists of youngsters, still living at home, being cared for by their parents, sometimes still in college or other education, sometimes already working, but in most cases with at least a part time job enabling them to earn some money. This money are extra savings because they do not need to spend it for housekeeping, living, and such, and thus, so to speak, saving money for the day that they would leave the nest. Most of these youngsters have a boy- or girlfriend in the same situation – still living with their parents – and thus doubling the amount that is being saved. When leaving home, in many cases to marry or live together, the people from this segment will probably opt for an own house, because, as the team later learned, this is what they are used to; their parents are house-owners themselves. One of the other learning later on was that the parents of these youngsters donate their children some extra cash when leaving house.

The second segment consists of mainly single young people, already on a well paid, but also demanding job, that want to leave the parental house as quickly as possible, and own their own place, to be, as we later learned, independent from family and to show off this independence status to friends.

The last segment identified consists of older starters, that have been living in hired house for a few years, in most cases with a partner and a kid or the wish to have children. For this reason, family expansion, they are looking for an own place, where they can have more children and live a family life like most other couples do. Often, both partners have a job and therefore a double income, making it easier to acquire a new house and a mortgage. The difficulty lies in the fact that having kids would probably mean that one of the partners has to quit the job or work less to give the children a proper education, making the sustaining redemption of the mortgage impossible.

The next step entailed a focus group session for each segment to further understand the needs, the motives for having an own house, the strategies that the consumers made to finance their ambitions. For each focus group session five to six participants, representing a member of the segment looking for or on the verge of buying a new house, were invited for an 2 to 3 hours discussion in an evening with the project team members. Participants received a monetary incentive for this. The session identified several – varying from six to ten per segment - consumer insights for the project objectives. But it also helped the participants to learn from each other; they were all peers in the same session, but everyone had his or her own strategy or tactic to acquire a new house, which was in some occasions an eye-opener for other participants.

The project team also observed all participants closely on their coping strategies, their creativeness and inventive ways and means to fulfil their needs on the subject. From each segments one participant was identified as a 'lead user' [26], and was later on invited for a co-creation session with the project team. In this co-creation four more bank employees – marketers and product specialists – were invited, totalling a number of 13 participants. This co-creation session was held about two weeks after the focus group sessions, and was intended to generate some useful product and service ideas to be developed. The session took about six hours, with a lunch break, in a creative environment, where nobody could be interrupted for daily business. In this session the participants jointly created , based on the insights acquired through desk research and the focus group sessions, personas for each segment, brainstormed on ideas to handle these insights and persona needs, discussing these possibilities and translating them in service and product ideas. The session ended with a selection of the best and feasible ideas, on which the participating consumers could reflect concerning their own needs. The whole session was done in an interactive manner, with the aid of simple tools like mood boards, magazine pictures, markers and post its, and common techniques like brainstorming, open discussion, and voting. The composite picture in **Error! Reference source not found.** gives an impression of the session and the tools used.

Fig. 2: *Impression of a co-creation session with consumers*

Based on this session the project team was able to work out some propositions for each segment. These propositions were presented to a decision board, constisting of senior management in the bank. Only a few alterations in terms of estimated revenues and communication style were made by this board, confirming that the project team was on a right track. Five were selected to be developed. The selected propositions were also presented to other product specialists, and to the people that are going to sell these new financial products, namely the financial intermediary advisors, to check the underlying assumptions in these propositions. These intermediaries are independent advisors, with offices and operating in all regions of the country, advising consumers on all sorts of financial products of almost all insurance companies. These advisors can also be viewed as customers of the insurance companies. This check pointed out that these assumptions were correct and that the advisors foresee a success for these new products. Only 5 months after the project start two from the five propositions were ready for launch. The reason that the other three had not seen daylight yet was because of tax complications, international standardization legislation, and competitive motives.

5.2. Case study #2: promises in insurance

The second and last case presented in this paper is about customer involvement in the development of a brand communication for an insurance company. As has been argued before, consumers have a low interest in financial problems and solutions. The insurance company had the ambition of making the insurance process and product understandable, enjoyable and transparent for their customers.

First a ZMET® research was performed with 14 participants – consisting of consumers and small-business owners; half of them customers of the insurance company, half of them customers of other insurance companies. These participants were interviewed in-depth about their thoughts and feeling on transparency in insurance. The outcome of this research showed that people really wanted to understand the process, but were unable to do so because of several obstacles they perceived. Most of these obstacles were mere communication issues, like jargon by financial advisors, small print conditions in policies, and such, but in total making the whole insurance process a complete blur for consumers and business-owners.

Based on these outcomes, as well as the insights that the research gave on the needs, motives and desires people have when insuring something, a team of communication specialists developed about a dozen of so called promises the company was going to give to make the process more understandable and enjoyable for its customers. These promises were derived from the frustrations and obstacles that people had expressed in the ZMET® research. These promises were scrutinized carefully by a steering committee; eight promises survived this scrutiny.

These eight promises were then tested in a total of four focus group sessions, consisting of consumers as well as small-business owners, both customers as non-customers, for agreement and the formulation of the proof that participants wanted to see for these promises. For each promise the focus group discussed the way that the insurance company could show upfront that it was really going to live up its promise. An example was for instance the promise to keep claiming simple and not bureaucratic at all. This resulted in a proof that asked for trust in the claiming customer, instead of distrust, by not demanding bills or other proof of ownership when somebody issued a claim. Two promises were discarded, because participants judged them either too pushy or incredible. From the other six, one was reformulated in a way that participants valued more as a promise. For all promises about two to five proofs were identified.

This result was incorporated in the following steps of the brand communication development. The whole process took about 14 weeks, in the eyes of the insurance company a remarkable acceleration of the process that normally took a year or more.

6. CONCLUSION

It has been argued that FS companies in the Netherlands have been little innovative over the past decade, and that they develop new products and services mainly inside-out, that is, without taking customer needs into account. The reasons for doing this it this way are that consumers do not seem to be highly involved with financial matters, and a certain fear for failure or fraud when involving customers in this process.

It has been argued that low involvement of consumers in itself is a result of the way that FS communicate and develop their services. Evidence from other industries shows that customer involvement in new product development enhances the chance for success of the new product, so we may conclude that FS can benefit from involving customers in their innovation process .

The two presented cases substantiate this conclusion and show us that the time-to-market as well as the quality of the innovation can be greatly improved.

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