WHITE PAPER

FINTECH – A BOOST TO BANKING INDUSTRY

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Introduction

COVID-19 is reshaping many business models to deal with the challenges due to the unprecedent environment, changes in customer behavior and expectations. There is a sudden surge in online payments and payments through third parties due to limited physical contact, social distancing and spike in e-commerce across countries. **Starting from supermarkets to convenience stores all are in a rush to go online thus creating an immense opportunity for the banks.** As per recent research done by The Financial Brand -

- Since Covid-19, more than 45% of respondents show a change in the way of their interaction with their banks showing a measurable shift away from cash and checks towards contactless banking.
- 45% of consumers have used a mobile wallet payment platform.
- 31% of respondents will use online or mobile banking more in the future.

Banks are taking substantial steps to ensure business continuity as well as the safety of their employees and customers. The pandemic situation has established that there is immediate need for banks to introduce or improve digital channels for their products and services. It's time to be more resilient and banks will need to adopt new strategies to bridge the gap. Banks should look forward to **reducing time to market**, by adopting new digital or cloud solutions that could help them to address the current issues caused by aftermath of COVID-19. This is an opportunity for banks to revisit their current strategies and move forward. Innovation is the future and partnering with Fintechs will help Banks to fast forward to next-gen banking. Though this is not an easy move as it will require a careful and well thought off approach. Banks would need to ensure there is no stone left unturned in this process and consider this as a bank wide exercise. However, the critical question would remain, which Fintechs to be preferred and what should be the alliance strategy?

This paper elaborates on current **FinTech adoption trends** and how it is evolving as a common strategy in the banking industry as a reaction to the current crisis. The paper also explains why the new generation Fintechs aka New-Gen Fintechs are getting special attention and priority from the banks during this current period.

Challenges in current banking landscape

1. **Increase in competition due to increase in digitization and rapid growth of new technologies**

   Fintechs have an edge over conventional banking due to usage of modern-day technologies. This is leading to Fintechs acquiring vital areas and processes of Bank's turf instead of Fintechs working just as a support for banking services. For e.g. As per an article in BankingDrive.Com, American Fintech Credit Sesame acquires Canadian challenger bank stack by integrating its credit services with Stack's digital banking in order to bring cash and credit management to Canadian consumers.

2. **Need for secured and integrated banking platforms**

   While banks are improving on **customer experience, security** is one aspect banks are looking to further strengthen with technology support in this space. In this area **biometrics, face-match, photo identification, digital signature** and technologies like **video-based identification** are on the definite priority list for the banks.

3. **Lack of Personalized banking experience**

   Personalization in banking is becoming increasingly important. From product recommendation to complaint resolution, reaching out to customers though their preferred channels to helping customers building their portfolio as per their own need are some examples. These features are still missing to a large extent across banks and hence banks are still not able to meet the customer expectations fully and thus it directly impacts the customer satisfaction / NPS scores.

4. **Slow technology adoption and innovation**

   Today's digital world has less room for manual systems and processes. Many banks are still struggling with manual and paper-based processes, operations folks still deal with manual steps or tools in silos. Verification of data is still dependent on how accurately staff are performing the task. Complaints and queries ending up in wrong queues and taking immense amount of time to respond. Still to a large extent, banks are a way behind in adoption of complete adoption of technology and innovation.

Approach towards a fintech ecosystem

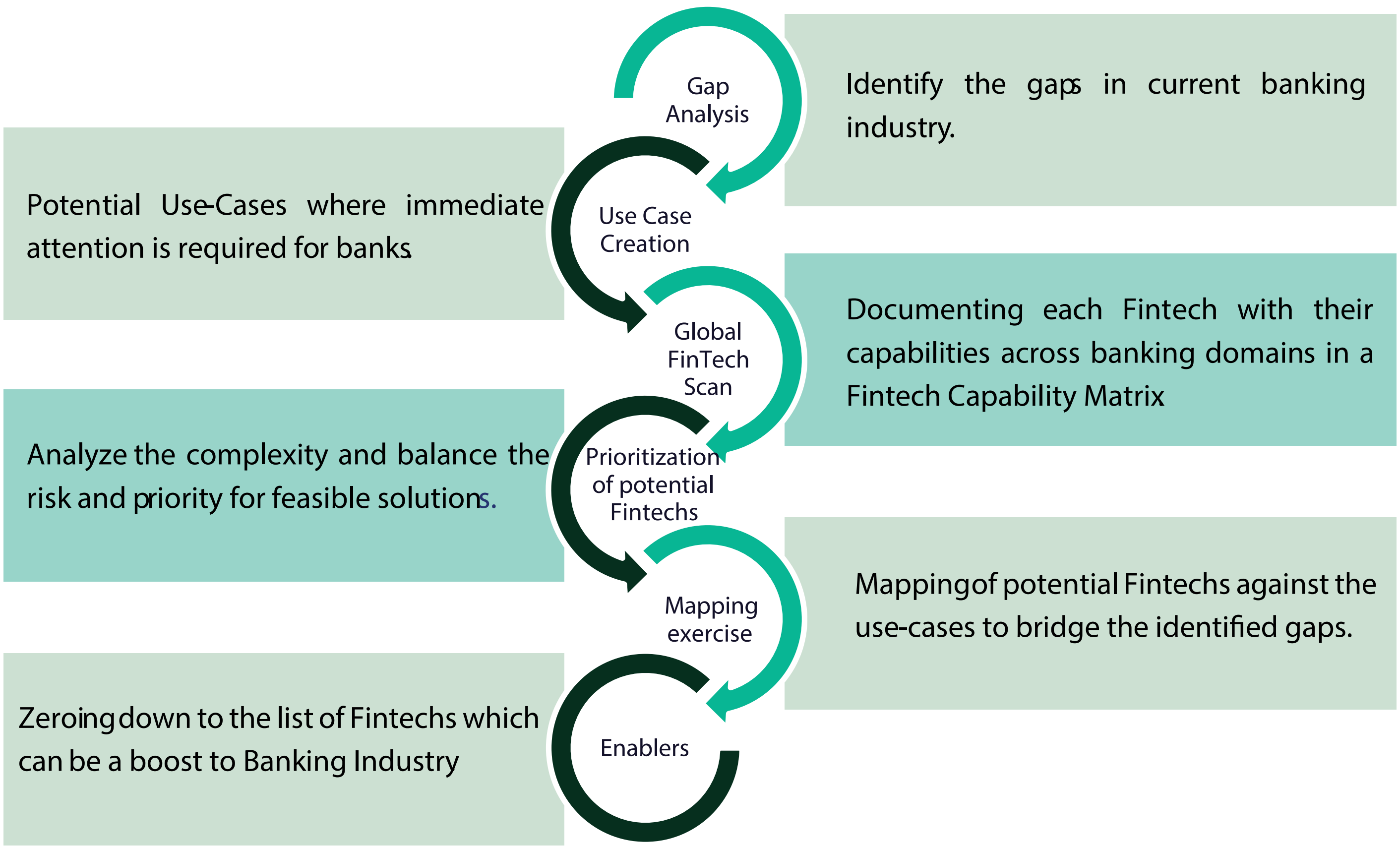

Fig1: Fintech Ecosystem focused on Future Banking

Adoption of fintech across the world in banking

The rate of adoption of Fintech in the Banking industry has been on the rise. Given below is the adoption rate of FinTech across the globe, showing the evolution of Fintech over the years and how different geographies have adapted to this. There has been an increase in the average FinTech adoption in 2019-2020 across the globe from 34% to 64%.

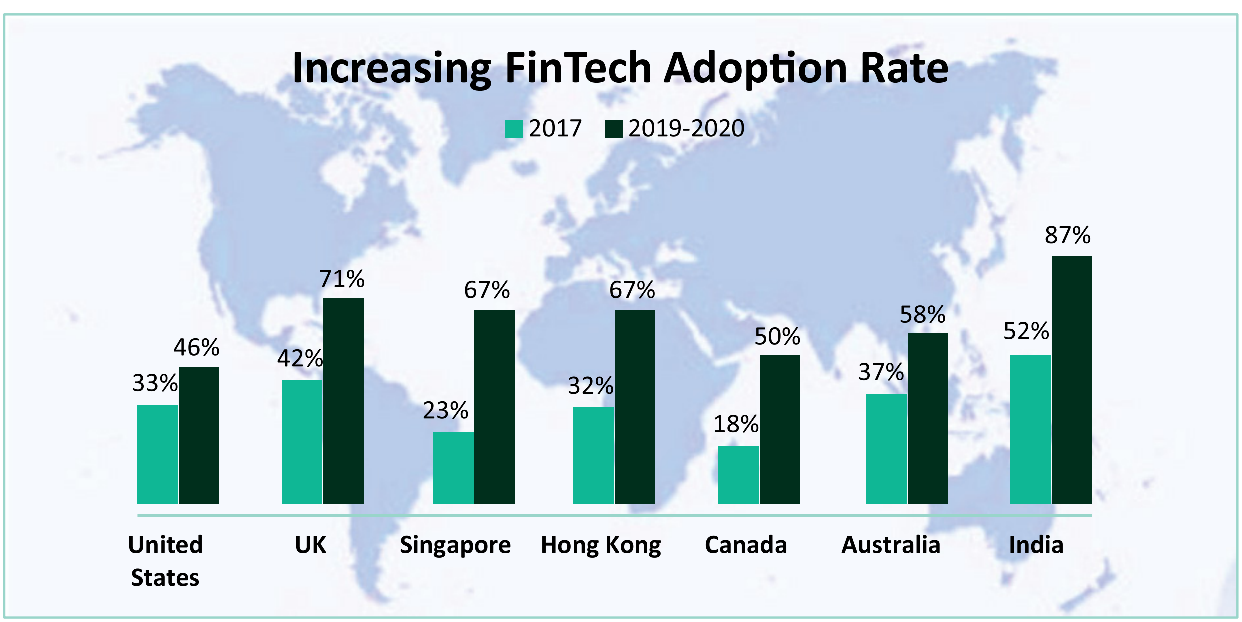

Fig 2: Fintech Adoption

As per the EY-global-fintech-adoption-index-2019, adoption rate across various domains of Banking and Financial Services from 2015 to 2019 is as below: -

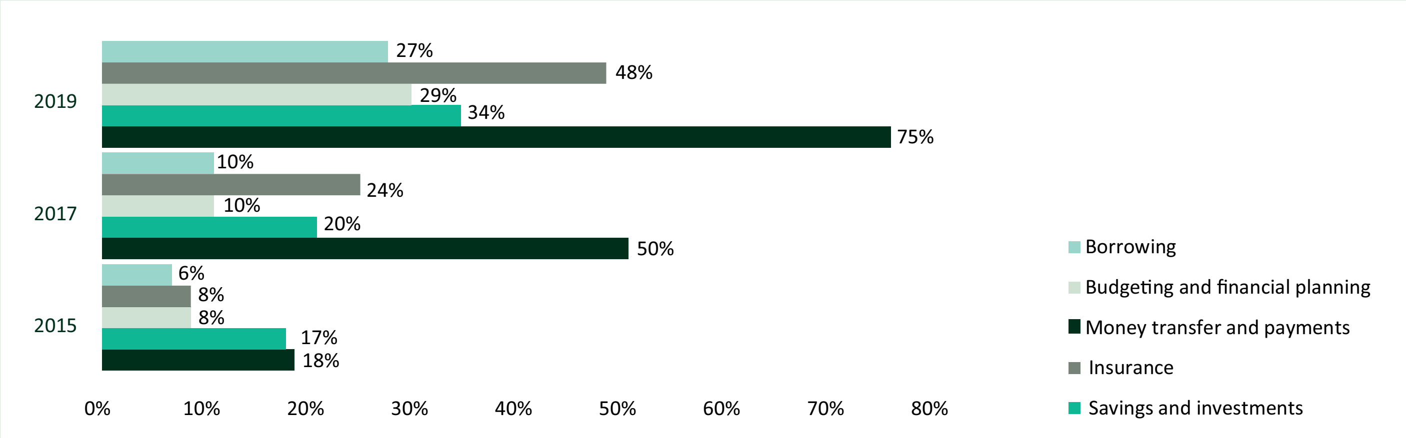

Fig 3: Fintech Adoption as per various banking domains

Fintech- a boost

Financial Technology, commonly known as FinTech are the new age startup and emerging companies that have leveraged advanced technologies and are disrupting the traditional Banking and Financial Services industry. FinTech products are often unique in nature. Typically, FinTech identifies an industry problem and focuses on that area to offer solutions that could turnaround the efficiency and customer experience to a superior level that was never realized before. FinTechs utilize point solutions, cutting edge technologies, algorithms and software which helps banks to improve their processes and operations. The channels of banking services are getting leaner and accessible from different devices such as smart phones, tablets, IVR and wearables thereby bypassing the visit to branches.

Banks have been offering a broad range of traditional banking services from payments, lending, deposit to investment services. A Fintech focuses on a specific functional area and enables the individual offering with enhanced customer experience or simplified digital process using cutting edge technologies. This will eventually help the bank to perform better in this competitive market and enhance their market share.

Fintechs are transforming critical conventional steps to completely online and automated mode from check processing, credit decisioning, onboarding, transaction monitoring, fraud surveillance and many more. Fintechs are also helping to meet customer expectations empowering customers to have a strong grip over their financials and enabling them to self-service which leads to a greater financial literacy than before.

New-Gen FinTech accelerating banking industry

The new generation Fintechs are into cutting edge technologies like AI and ML, Blockchain, Cloud computing, Deep learning etc., focused on having easy access to open source frameworks, scaled cloud computing and development on-demand. These are more streamlined in their approach with an ability to innovate quickly, taking advantage of the opportunity to fill the gaps.

These New-Gen Fintechs are redesigning the processes with their high-end technology expertise, aimed to apply technology to improve financial activity. We have seen a significant growth in payments, lending, security and biometric segments. It provides an end-to-end business model with products, solutions, processes etc. They deal in various areas of Banking like product solutions starting from digital onboarding, global payments, fraud prevention, risk management etc. These FinTechs provide various solutions to all merchants around the world to help them to cut down their costs, increase their conversion rates, mitigate frauds and enter new market segments.

Banks are finding it difficult to sustain in the environment by keeping pace with increased regulatory changes while keeping an eye on their operational efficiency. Hence banks are looking to adopt the newer technologies, innovations and agile business models. Newgen FinTechs are helping banks to align with their strategic choices thereby providing a product and solution within their capability.

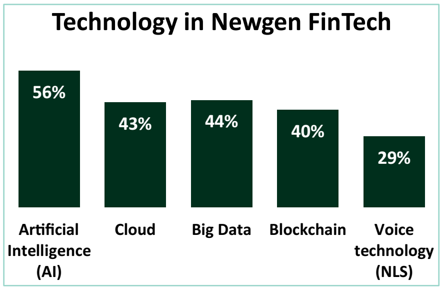

Fig 4: Most adopted technologies by the New-Gen Fintechs as per pwc-global-fintech-report-2019

Bank's journey with FinTech (Conservative vs Collaborative approach)

Banks have their own strategies, capabilities and technological competencies. The Big Techs (Amazon, Google, Facebook, Apple) are also disrupting many banking services and one such area of disruption is Payments. FinTechs on the other hand have some cutting-edge technologies as an advantage. Banks have enormous amount of historic data with them, be it customer data, transaction data, behavioral data, analytics and more. FinTechs operate in a limited scale and budget. Banks are looking to re-strategize and collaborate more with FinTechs which can result in quick benefits, enabling banks moving from a traditional banking world to a Digital Banking world at a faster pace.

Some of the benefits of striking a partnership between a Bank and a FinTech are as below: -

- **Cutting Edge Technology** – In this era of stiff competition, banks having a collaboration with FinTechs will have an advantage over conservative banks due to latest technologies.
- **Plug and Play Solution, Swift TTM (Time to Market)** – Quicker TTM as FinTech provides policy and regulatory related solutions to banks.
- **Focus Driven Products** – The products and solutions offered by a FinTech against a single problem identified for e.g. digital onboarding, conversational banking etc. is focused for a very niche area using latest technologies.
- **Transaction at Ease, Reduction in Processing Time** – As per banks' perspective, transactions using latest technology will save time, effort and money.
- **Regulatory Compliance** – Adheres to all latest regulations and hence banks find it easier to adopt and collaborate with FinTech without worrying much about the regulatory impact.

How new-gen fintechs bring a difference to the banking industry

New-Gen Fintechs have transformed the banking space with various products and solutions. There is definitely an edge when banks join hands with existing established FinTech. New-Gen Fintech not only focuses on customers but also leverages their creative product and solutions towards regulatory frameworks, government policies, security perspective etc. It's creating an ecosystem where it engages with banks and financial services companies with Partnerships, Mergers and Acquisitions. Several jurisdiction and regulators are seeing a potential in these New-Gen FinTechs and have supported them with various initiatives and hackathon events.

This has opened opportunities for banks in identifying the right FinTech and partnering with them. Traditional banks are not designed to think and behave like other modern tech companies given their current burden of legacy processes, products and regulatory compliances. The technology like AI, ML, etc. gives much refined customer experience and reduces exposure to risk. New-Gen Fintech offerings had given banks a new way to engage with customers more efficiently and with a quicker response time. Their agility working model provides a better end-to-end solution and faster time to market.

Banking industry is preferring New-Gen FinTech over an established one's, as New-Gen Fintechs are more into cutting edge technology, offering is responsive, able to serve and adapt to emerging customer needs faster, provides a wider architecture, security platform. New-Gen Fintechs are basically focusing the untouched banking areas. Some of the New-Gen Fintechs are Signzy, Neener Analytics, Lemnisk, Glia and many more which show to play a significant role.

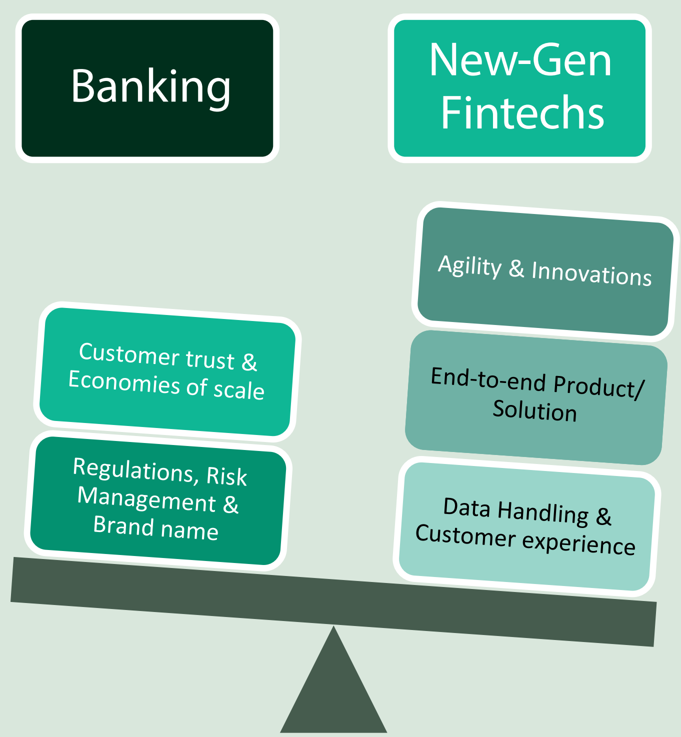

Fig6: Balancing Banking with Newgen Fintechs

Success factors for banking industry

The key success factors banks need to evaluate and pay attention for alignment with FinTech are listed below.

Strategic Partnership

Current challenges in banks to a large extent need technology support which is beyond the capacity of bank's resources and available time. Hence, it's important for banks to not only collaborate with FinTech but also make them a partner towards their larger goal. Banks need to build strategic partnership and work as a team with one specified goal. A joint vision, process and specific goals with binding legal obligations need to be clearly defined as part of strategic partnership agreement.

Partnership Structure

A FinTech partnership structure helps to define the limitations and obligations of each party. This helps to clear any ambiguity on revenue sharing or profit from the future achievements. A partnership could be one of the many types such as Referrals, White Label Solution and Buyout or Outright Purchase.

i. Referrals: Banks avail FinTech services for category of customers who are seeking high-end personalized services. This is more applicable when specialized services are offered to a subset of customers and probably works as a revenue sharing based model.

ii. White Label Solution: Bank subscribes or buys the services or product offered by the FinTech as a white label solution. The solution could be deployed on bank's own premise or to cut cost and get rid of future maintenance, banks can also opt for cloud-based software as a service (SaaS). In this case pricing of the solution is often on subscription basis or transaction based which is also known as 'pay as you use', which is the most cost-efficient way for banks to leverage these kinds of services.

iii. Buyout or Outright Purchase: Banks have another option where they could go all out and acquire the FinTech. In rare cases, banks even just buy the solution exclusively which means the right to the solution will be transferred to the bank.

Success Measures

Strategic partnership should clearly describe the success measures for bank as well as Fintech. Each party should have proper alignment with the expectations and ownership of the deliverables. A dynamic and strategic plan in place is absolutely necessity for process measure and will act as a driver.

Cultural Melding

Melding distinct culture of FinTech and bank is critical for their success. Working culture and development environment are totally different when it comes to traditional banks vs the startups. Therefore, this is critical to avoid any cultural pitfalls and remain focused on the outcome.

Measures towards risk mitigation while collaborating with fintech

Data Security Risk

- Banks need to be careful when services are hosted on a cloud while integrating with Fintech services as they deal with customer sensitive information and transaction data.
- Presence of a legal agreement between the involved parties defining the type and extent of data that can be accessible by a Fintech is required.
- Banks need to ensure certifications such as ISO 9001 (Quality Management), ISO/IEC 27001 (Information Security Management) etc. are in place to be compliant.

Financial Risk

- Banks need to have clarity on various pricing models offered by Fintech along with the terms and conditions of the contracts.
- Banks need to get into an agreement which provides clarity on YOY increase of pricing, if any, to help reducing the financial and operational risks.

Cultural Risk

- Banks need to select a Fintech through in-depth evaluation of its value proposition, geographical presence, compliance limitation etc. in similar engagement.
- An alliance would need to ensure both parties understand and are ready to step into each other's shoes towards the common goal.

Creativity is the way forward

Banks need to be extremely creative and assess if a strategic partnership or acquiring FinTech will enable them to offer creative solutions. Tech savvy, mobile users, the millennials and Gen Z are the new target segments for banks and hence they need to satisfy their needs and expectations and retain their relationships. API driven creative services focusing on customer experience is becoming the way to go. Banks like JPMorgan are already taking steps with digital only bank and planning to acquire Fintech E*Trade to reduce their cost.

A FinTech, LendingClub has pioneered peer-to-peer loans, offering digital personal loans completely online. In just 14 years the San Francisco based FinTech has become a competitor for the banks on its own. In 2020, it's now set to acquire a US bank i.e. Radius Bank. This might become a frequent phenomenon going forward unless incumbent banks take the right move strategically.

It's not too late for banks, COVID-19 is a good opportunity for the banks to test the resilience and start identifying the weak nodes. Many technology services companies with existing relationship with banks started analyzing bank's technology landscape in identifying the right fit. These organizations are helping banks as a common link to bridge the gap. It's often a good idea for the banks to leverage existing relationships and leverage external consulting in the right alignment with the FinTech.

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Conclusion

In this disruptive and competitive market, banks need to evaluate 'build vs buy' at every stage of their technology investment in any initiative. Banks should start considering New-Gen FinTechs in their priority business areas. New-Gen FinTechs can be considered as a booster to their existing offerings. This can help them align with their goals of customer delight, increasing NPS (Net Promoter Score) and reducing time to market new products and services. For a bank it takes enormous time, effort and money to build a customer base and hence a careful analysis is required while finding the right fit New-Gen FinTechs for a bank. Hence bringing the New-Gen FinTechs onboard and sharing necessary information is much needed for a strategic alignment. Last but not the least, a mutual trust needs to be built between bank and FinTech in order to drive the common goals as a team and boost customer experience.

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