I Love my Bank

How the Digital Revolution in Banking is Transforming the Customer Experience

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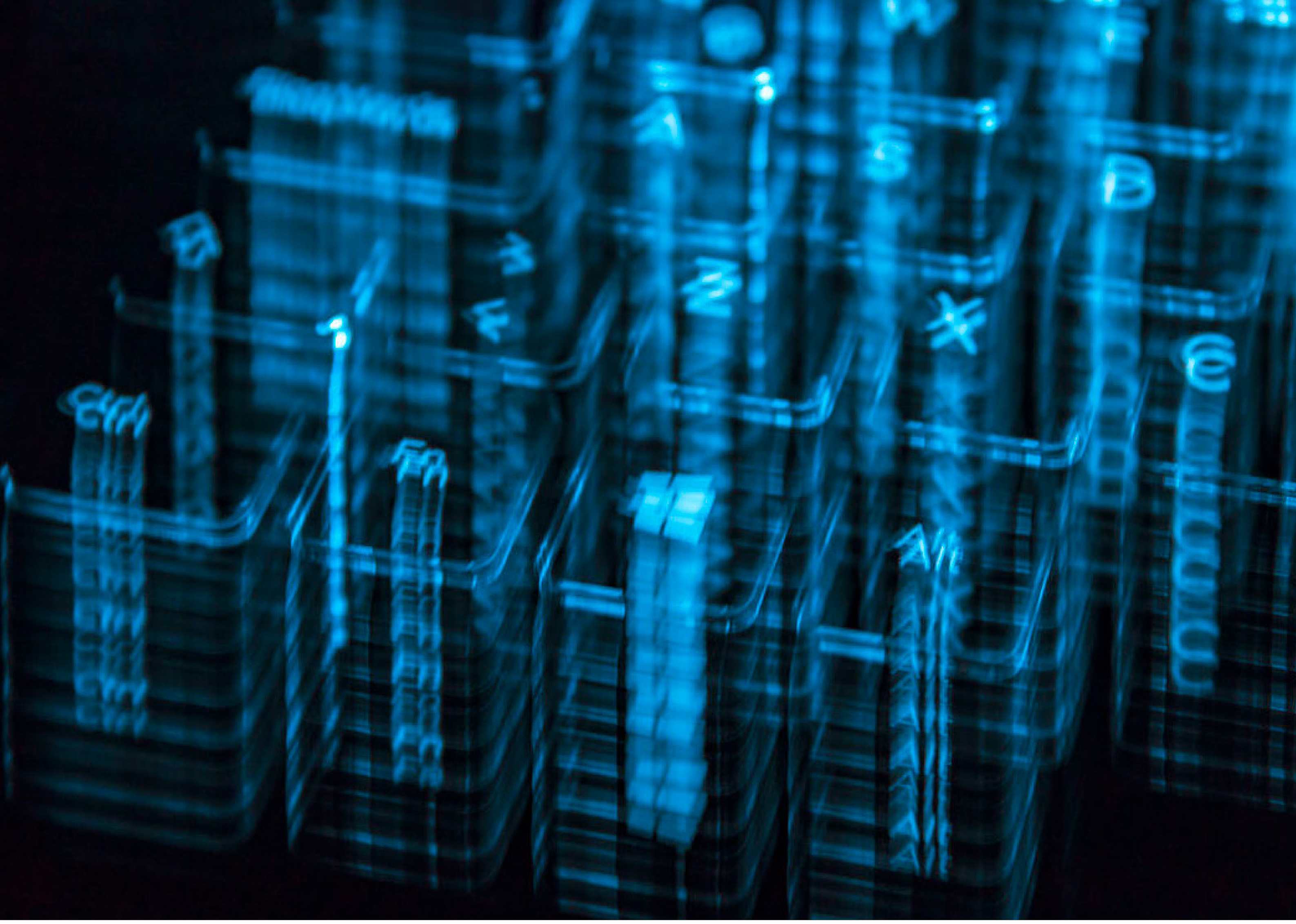
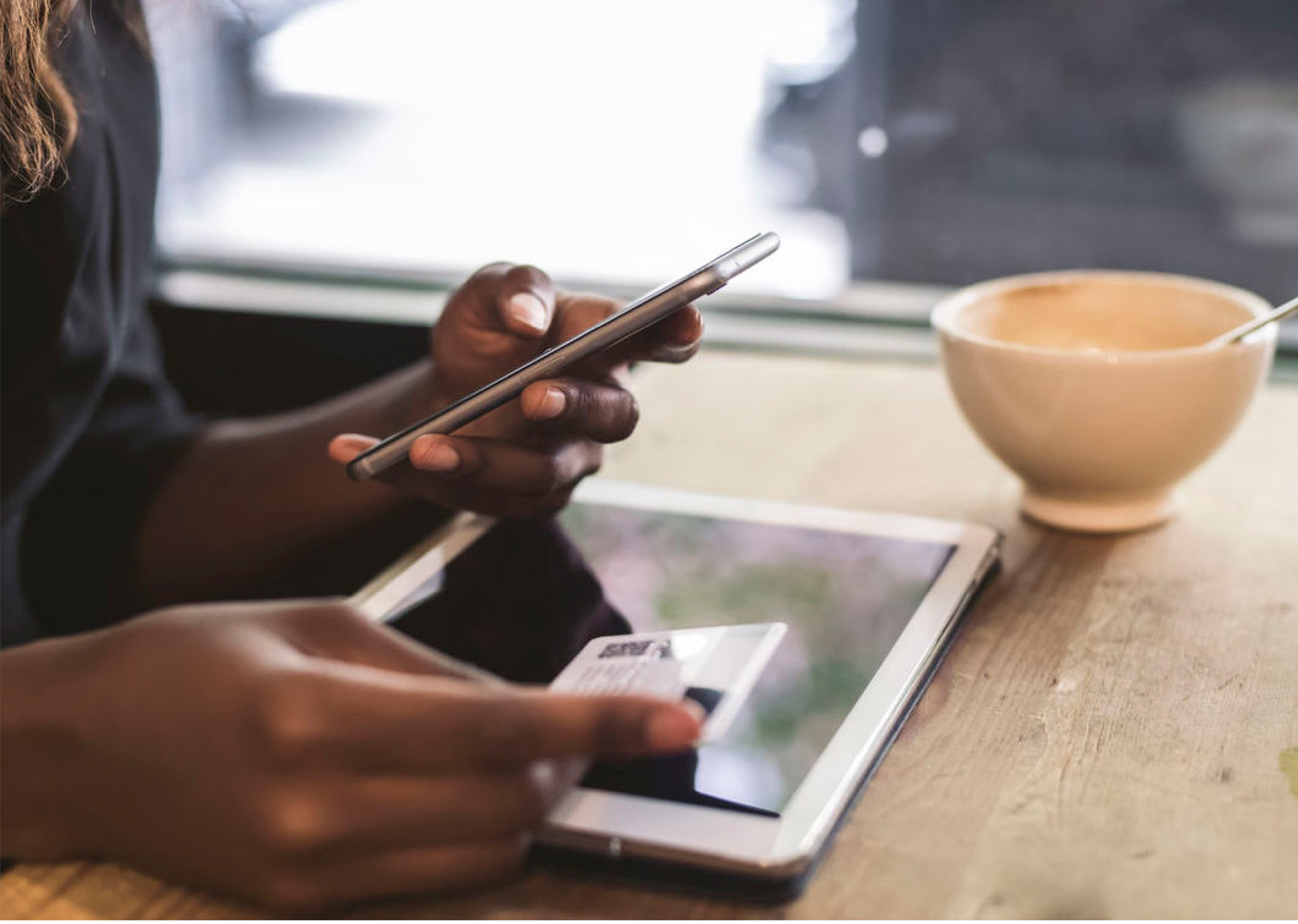


Executive Summary

Retail banking in South Africa is increasingly competitive with neobanks and digital players entering profitable segments across the banking value chain. For banks to be loved by their customers, they must reimagine their customer service – with continuous innovation required to meet customers' evolving expectations. For some players, this requires a holistic digital transformation to reform legacy systems and processes. For most, it will mean assessing their existing and future business models. For all, it will require leveraging customer data to personalize engagement and better predict and exceed customers' needs.



Increasing pressures on retail banks

Incumbent retail banks face pressure on several fronts, including from digital challengers, like Discovery Bank, Tyme Bank, and Bank Zero, as well as tech players that are disrupting the banking value chain. These digital players are driving increased usage of new financial technologies that lead to an unbundling of the banking value chain. This trend is likely to continue as these disruptive technologies mature in the financial services industry. Incumbent banks must respond if they are to maintain their leading role in customers' financial journeys.

If retail banks want to be loved in the future in the face of these changes, they will need to meet and exceed the evolving expectations of their customers. This requires giving customers what they want when they want it. Serving customers in this way requires a clear understanding of the customer, strong digital interfaces, holistic solutions, and modular products that can be adapted quickly to meet the needs of the customer. Key to achieving this will be leveraging customer data and building the data sets to provide fully personalized offerings that anticipate what the customer needs before the need arises.

South African consumers' preferences are changing. The majority believe there may be no need for banks to have physical branches in just five years. Branchless banking already exists in several cases, such as the models for Discovery Bank, Tyme Bank, and Bank Zero. Covid-19 has accelerated the adoption of digital channels and transformed the way customers want to interact with their banks. ~80% of customers have expressed a preference for conducting their day-to-day banking digitally, while ~60% of consumers say they would be comfortable with a completely digital full-spectrum banking offering. More consumers will potentially use digitized services given greater digital access and confidence that it will be easy, efficient, and safe.

Our recent article, the Future of Retail Banking, found that not all incumbent banks are fully ready for the transformation to digital banking. Some are encumbered with legacy IT infrastructures and processes, while most have brick-and-mortar bank branches with capabilities ill-fitted to the digital world. These incumbent banks must reinvent the ways they address customers' needs and pain points. If not, they may struggle to maintain their customers' love and remain the preferred port of call for financial services.

Retail banks are in a competitive starting position but will need to adapt. They benefit from high levels of customer trust, strong brand awareness, and skilled staff. This can play an important role in an omni-channel customer relationship. But without change, incumbents face separation from customer touchpoints, losing access to customers and valuable data in the process.

Increasing pressures on the retail banking industry

Demanding consumers

- Responsiveness & convenience
- Relevant personalized offerings
- Financial inclusion

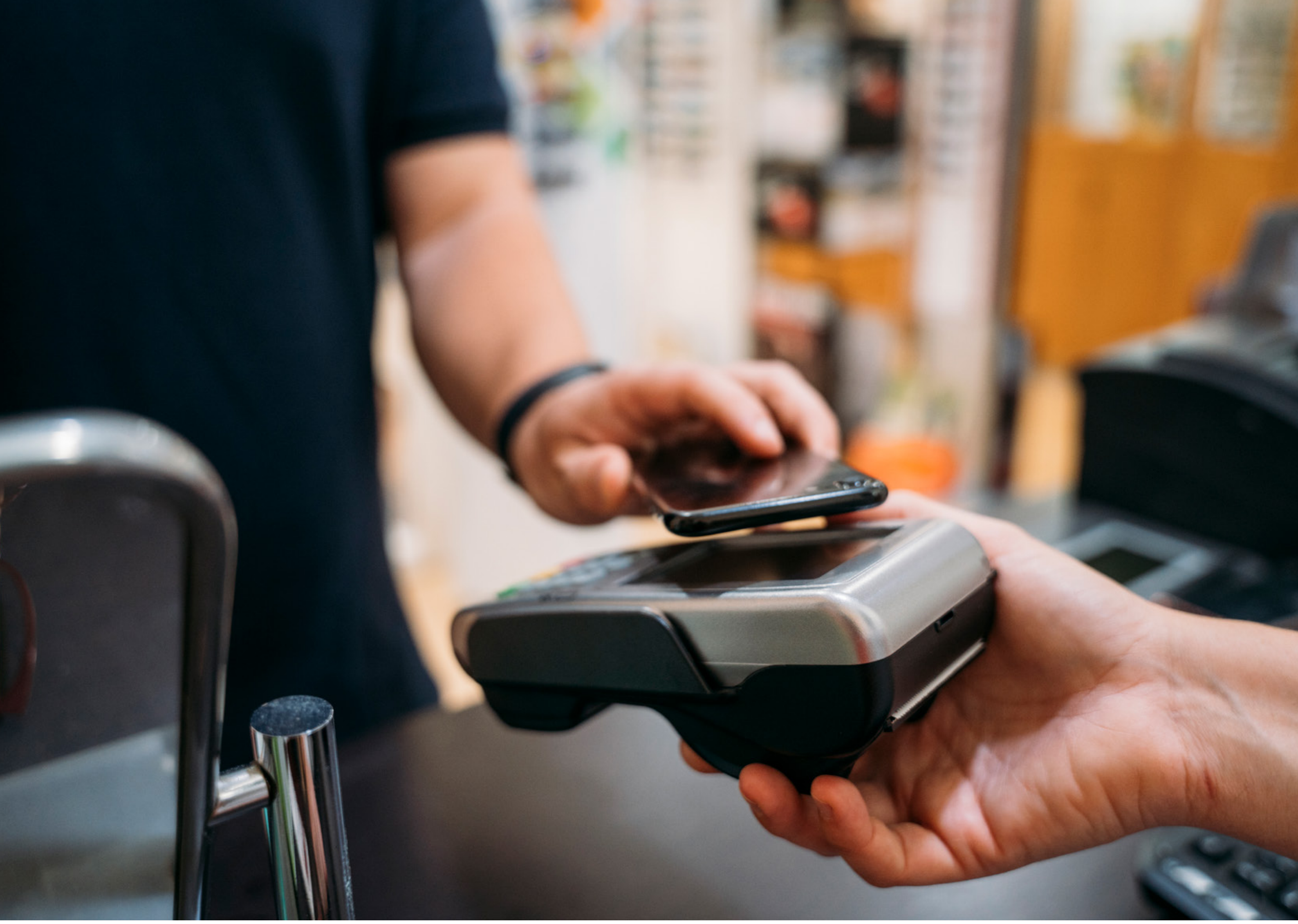
New competitors

- Digital banks, neo-banks
- Payment specialists
- Tech-fin – technology giant + ecommerce platforms

Market conditions

- COVID-19 recovery
- Market and geopolitical conditions
- Increasing cybercrime

Need for incumbent banks to **address customers needs and pain points innovatively**



Digital is more than an app

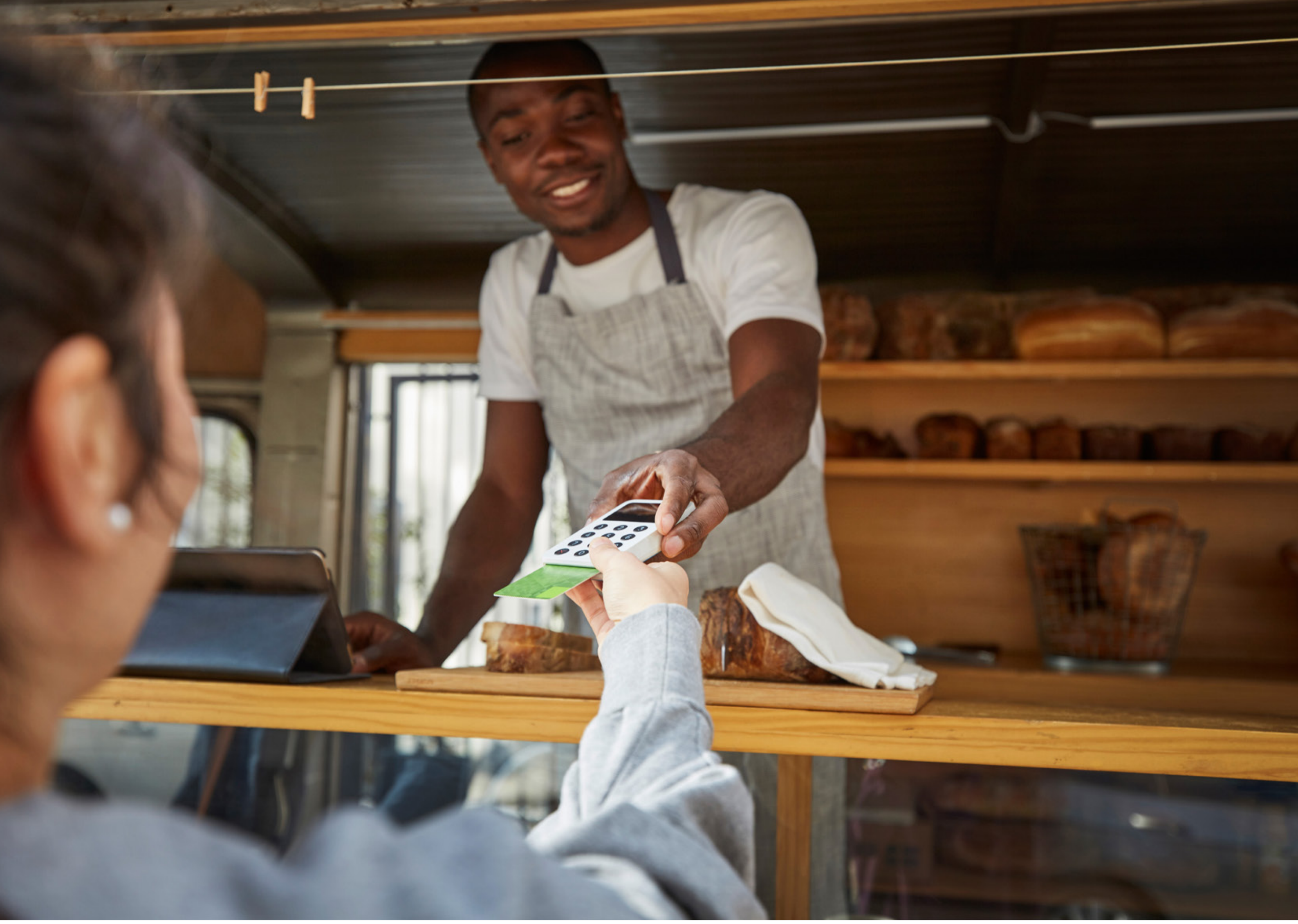
Digital channels are now much more than avenues to reach and serve customers. Rather, they are transforming the way people interact with money and financial services. Banks no longer have the sole right to banking relationships with customers. Increasingly fintechs and telcos are entering profitable segments in the banking value chain offering new, attractive digital banking services. In the future, the widespread use of digital banking services by customers may necessitate collaboration between banks and fintech players. Without collaboration, banks may face disintermediation and loss of access to customer data.

To understand how customer needs might evolve it is instructive to look to China. There are indicators that African markets are more likely to follow the Chinese model than paths followed by Europe and the USA. African customers experience friction with the financial system and financial inclusion remains limited, similar to the starting point for China's market. Additionally, with a young and digitally savvy customer base, digital adoption is rapidly increasing across the continent. China is further on the journey than Africa, but we are likely to see similar collaboration between banks and fintechs.

In China or example, WeChat, Jimbox and Rong306 have been at the forefront of this disruption, leveraging high mobile phone and internet adoption to address deep-rooted limitations in customers' banking experiences. In South Africa, increasing mobile phone and internet penetration together with continued challenges inhibiting financial inclusion, create the ideal opportunity for fintechs, telcos and tech players to exploit. Unlike China, South Africa has no domestic social media and internet players, but telcos and fintechs are a risk to incumbent retail banks' hegemony. If incumbents fail to change the way they serve their customers' needs, digital financial services may threaten the very existence of banks in their current form.

Despite the threat posed by these new players, we believe there is a space for both incumbents and challengers. Incumbents are advantaged by their large, relatively stable customer bases and high degree of trust. This enables them to leverage customer data to better understand and address customer needs. However, challengers have their own advantages by focusing on selected (profitable) market segments and developing tailored digital propositions for specific customer journeys. Challengers also do not have to worry about historic client churn, digitization of legacy processes, and change management to transform their operating models. Nonetheless, challengers do still need to innovate continuously and offer new and improved customer offerings to keep pace with changing customer expectations.

Incumbent retail banks have begun to respond to the threat. Some have begun by modernizing their IT systems, while others have reassessed their operating processes, and the way they serve customers. For example, First Rand, Nedbank, Standard Bank, and Absa allow customers to obtain full home loan approval using their digital channels. Additionally, they incentivize using mobile channels by offering cashback and discounts on mortgage bond application fees.



What can incumbent retail banks do to reignite customers' love?

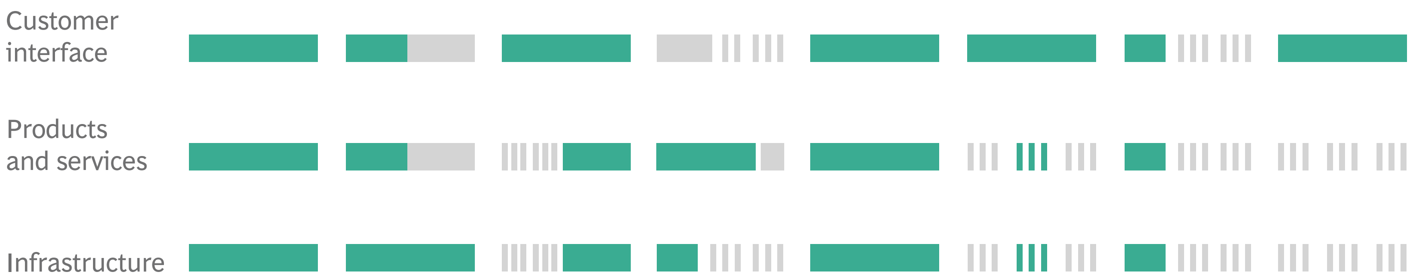
Incumbent banks need to redefine their approach to customer interactions if they are to retain their position as the primary hub for customers' financial needs. Instead of looking for new ways to deliver existing services, incumbents should reinvent and expand their services to address customers' key pain points and needs. By doing this, incumbent banks will be able to retain the primary customer relationship. This could lead to an increase in the frequency of engagements, access to new data, and maintain customer stickiness. Retail banking is not a one-size-fits-all proposition. Incumbent banks will need to decide on a business model that best suits their customers' needs and maintains a loving relationship between the bank and its customers. To win in the future, players should consider adopting one of several viable business models.

We see eight future business archetypes to win in retail banking in the future

Possible evolution of incumbent business models: Digitised Full-Service Bank, Open Bank, Ecosystem, Product Engine

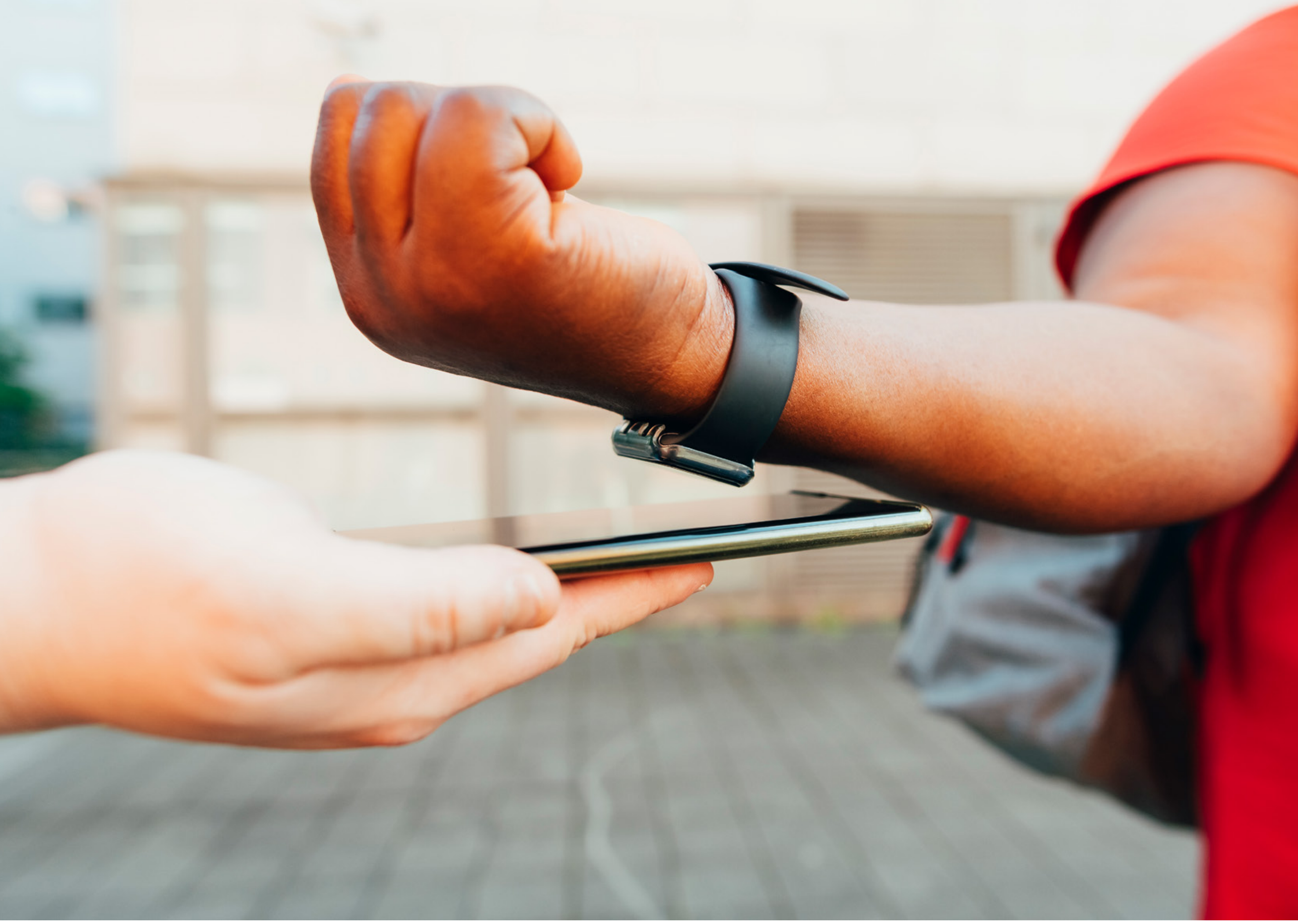
Attacker business models / New digital growth option for incumbents: Ecosystem, Product Engine, Direct Bank, Neobank, Specialist Provider, Marketplace

Digitised Full-Service Bank	Offers closed catalogue of own products through own best-in-class digital channels and own branch network
Open Bank	Manufactures and distributes own products but extends reach by participation in marketplaces/ ecosystems
Ecosystem	Orchestrates products/services (including in non-banking customer journey) through extensive partnerships
Product Engine	Orchestrates products/services (including in non-banking customer journey) through extensive partnerships
Direct Bank	Offers features of Full-Service Bank but without branch network; primarily focused on securing deposits
Neobank	Built for mobile on new tech stack. Narrow product focus (e.g., transaction acct); imports products and services from third parties
Specialist Provider	Manufactures narrow range of products, typically focused on specific segments
Marketplace	Offers choice of products from competing providers, often across sector; first-class digital interface UX/UI



Source: BCG Analysis

In-house   Outsourced



Business models to seize the opportunities of digital banking

Digitised full-service bank: Offers a closed catalogue of its own products through its own best-in-class digital channels and branch network. In-person services are available upon request, and the bank is fully bionic, enhancing its human interactions with digital functions. Such a bank caters to customers by having a deep understand of its customers' needs and leveraging customer data to offer personalized services. Additionally, a strong digital interface and excellent execution ensures customer satisfaction.

For example, Lloyds Bank in the UK is investing in new sources of competitive advantage such as open banking technology and data analytics to meet the needs of target customers segments more effectively.

Open Bank: Offers its own products, but extends its reach through marketplaces and ecosystems, integrating its services with others. For example, this bank might partner with other banks, fintechs or neobanks to offer services such as account aggregation (US based Plaid and Swedish based Tink), or personal financial management (US based Mint). For open banks to be successful they need to ensure they have a strong interface, modular products that can be quickly adapted to meet the needs of customers and requirements of partners, and excellent execution to allow for a broad range of partnerships In South Africa, Spot Money operates as an open banking marketplace integrating virtual cards from other banks to create an interoperable payments app. Stitch, a South African API fintech, allows developers to connect apps to financial accounts. This allows users to share their transaction history and balances, confirm their identities, and initiate payments.

Ecosystem: Builds scale in its user base through extensive partnerships that offer a wide range of products and services, including non-banking features. The client might, for example, be able to use the bank's web portal or app to access travel or shopping platforms, and apply points accrued through bank transactions to other purchases. For this to serve customers' successfully, there needs to be a deep understanding of the customers' needs to predict what products and services to offer. Additionally, a strong interface and excellent execution is required to ensure ease of use for customers and to make the platform attractive for partnerships.

In South Africa, many incumbents have taken steps towards an ecosystem-centric model. Discovery Bank's ecosystem enables clients to book travel reservations and shop on retail platforms. Nedbank customers can use AVO to purchase products including groceries, home repair services, and appliances. First National Bank, through its eBucks platform, provides access to a wide range of retail, home, and travel solutions. Standard Bank offers Looksee, an integrated solutions platform for homeowners.

Product engine: Offers best-in-class financial products, mainly distributed through third party channels. A bank that wants to grow its lower-income customer base through a savings product could, for example, partner with a telecom company with access to that segment. To serve the customer needs, the product engine must have a modular design with quick adaption and be executed well to be attractive to third parties.

Sopra Banking in France specializes in ready-to-use tech stack for banks and other startups. This includes middleware solutions, community based-banking and other software solutions.

Direct bank: Offers the features of a full-service bank but without a branch network – transactions are all digital. The primary focus is on securing deposits, with account-focused services; for example, making payments. Such a business model requires strong interfaces, excellent execution and holistic solutions that are on par with incumbent banks offerings.

mBank in Poland, a market leader in direct banking, acquires and interacts with its clients mostly through digital channels. Its client base is largely under 30 years old, and university educated.

Neobank: Offers a narrow product range, focusing only on select high value product offerings, for example, accounts and payments only. But it might import other products and services such as forex trading or buy-now-pay-later financing from third parties. The neobank model is built to be used via a mobile app. Neobanks require a thorough understanding of customers' needs and pain points to be successful. Additionally, a well-executed modular design that is easily adaptable to changing customer needs and a strong user interface are key.

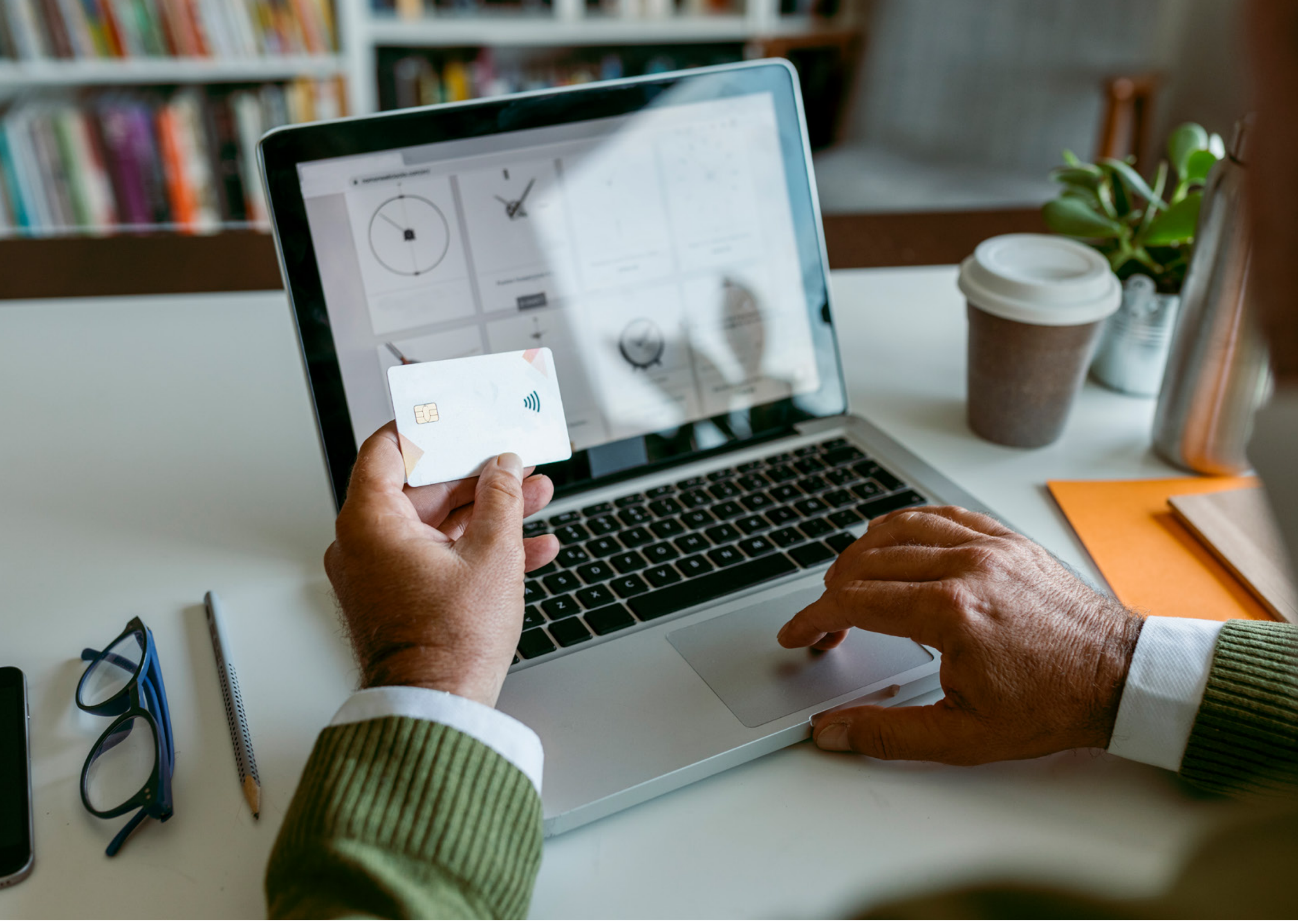
In South Africa, Discovery Bank currently operates as a neobank. It is focused on retail accounts, building on its existing lifestyle-based business proposition, but expanding to a wider range of products. Tyme Bank also operates as a neobank but leverages its partnership with a leading grocery chain to facilitate the opening of accounts.

Specialist provider: A neobank that offers a narrow range of products focused on specific client segments. Specialist providers in South Africa might, for example, develop a holistic niche market among the underbanked, or with small and mid-sized enterprises. Specialist providers meet customer needs by understanding the customer pain points and creating clear and well-executed solutions.

South African specialist provider Payflex is such an example and offers six-week interest-free deferred payments for consumers in eCommerce.

Marketplace: Offers a choice of products from competing providers, often across sectors, such as short-term loans or forex trading. It establishes itself as a go-to site for such products by giving customers a first-class digital user experience and interface. It has a clear understanding of customers' needs, a strong interface and excellent execution to draw customers to the platform.

British-based Money Super Market (MSM) has become a marketplace leader in financial products and continues to build its analytics capabilities so that it can offer more personalized recommendations to users.



Data analytics is key to customer loyalty

For both challengers and incumbents, the key unlock lies in data. In terms of the use of data analytics, the banking industry in South Africa is more advanced than other industries. Clear value has been derived from experimentation with data-driven use cases. This must now be scaled and expanded to include other solutions. The most value and focus should be on high-value use cases (unicorns) that are creating the most value. This includes identifying unusual spending behavior, identifying 'red flags' for loan applicants, and customer segmentation for marketing campaigns.

While incumbent banks may struggle to compete with tech companies on agility and core system design, they have several competitive advantages. Incumbents hold a position of trust with their customers. They have access to a vast database of structured and unstructured data that can be leveraged to understand customers' needs and address pain points better. Utilizing AI models, driven by customer data, will allow banks to draw commercially useful conclusions more quickly. This will allow incumbent banks to predict the needs of customers before they even arise. These predictive capabilities will create the sense that banks appreciate their customers' needs and are acting to ensure the best possible service.

Data also presents an opportunity to mitigate risk. Not only do data analytics streamline processes and tasks across the organization, but they also have tangible benefits for customers' and their experience with their bank. Customer data can be leveraged to detect fraudulent transactions and better understand credit risks and likelihood of full payment. This is not only a benefit to the bank but increases the customer's trust in their bank.

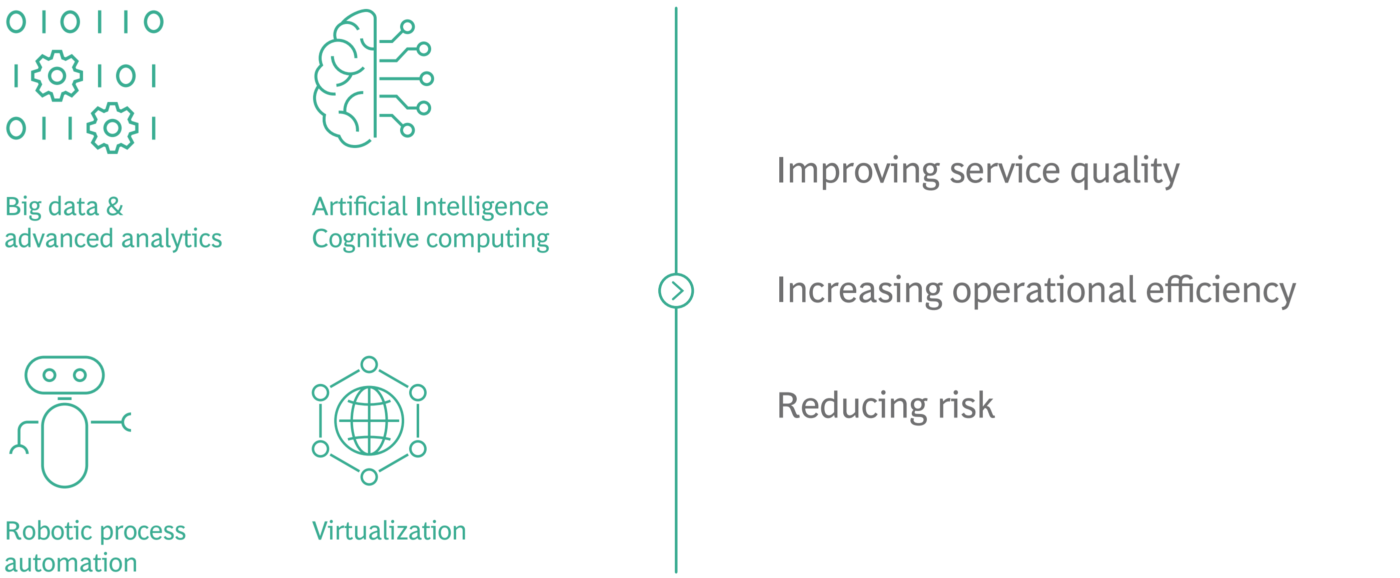
For digital players, personalized engagement with customer data underpins their plans to scale. For example, Discovery Bank entered the market offering personalized lending and investment rates based on spending habits. Of course, not all new entrants will be successful, but when one looks at the share of new business they already win today, it becomes clear that they are a serious threat to incumbent banks. Incumbents are fully aware of the opportunities presented by advanced data analytics, and many have taken steps to capture the opportunity to engage with their customers in a more meaningful way. In retail banking, there are six core use cases where customer data can be leveraged to offer better services.

- **Smart prospecting -** customer data used to generate 'pull' and offer precision outreach and engagement tailored to when the customer would be most receptive.
- **Smart engagement -** tailored offers and dynamic engagement at an individual level to significantly improve cross-selling, up-selling and onboarding.
- **Personalized journeys -** optimal cross-channel paths created for every customer and interaction to significantly improve sales and engagement.
- **Smart retention -** analytics used to identify and intervene effectively when customers are at risk of attrition.
- **Smart collections -** data analytics used to identify, target, and allocate collections resources to optimize costs and outcomes.
- **Personal financial health -** individual customer's financial health assessed based on spending and lending habits to improve financial outcomes over time

Many incumbents have begun the process of leveraging these opportunities to improve their customer engagement and better meet their customer's needs. For example, Standard Bank has been using data-led personalization to increase cross-selling of unsecured personal loans and

Maturing new technologies...

...offer an opportunity for banks to address profitability pressures



New way of working through personalization drives customer centricity

Traditional way of working		New way of working	
Product - led	"I have a Product, who do I sell it to?"	Customer-led	"I have customers, are they well served?"
Product campaign	"Which offer will appeal to most people?"	Relevant conversation	"Which of many offers will create the best experience for the customer?"
Manual waterfall delivery	"There are 20 active campaigns; I take 12 weeks to make a new one"	Agile digital delivery	"There are 1000+ campaigns; I create one in two weeks; I analyze performance every week"
Marketing team	"I do my best to serve the Product team"	Personalization team	"I do my best to serve the customer & bank; as an advisor to Product team"

improve customer retention. While all banks are investing in data analytics, many struggle to get value at scale. When they find it difficult to create proof of value quickly, they become more reluctant to commit to further investments. Existing efforts are often fragmented and come as a "push" by the technology function or from external service providers. As a result, they rarely scale past the proof-of-concept stage. To get impact at scale, banks should prioritize a limited number of must-win initiatives, anchor the responsibility firmly in the business, and set ambitious targets for measurable business outcomes. Getting it right requires strong business leadership and a new way of collaboration across many functions of a retail bank.

Banks that manage to transform the way they interact with their customers and create transparent and cost-effective offerings can reap substantial benefits in terms of both customer experience and financial performance. From what we have seen in European and American markets, the following results can be achieved:

- Number of touchpoints per customer can be doubled, churn can be reduced by 5-10%, and net promoter score (NPS) can be improved by 5-10 points.

- Together with more precise marketing and targeted use of channels, the above outcomes lead to top-line growth of 5-15%, a 30% increase in sales productivity, and a reduction of 20-30% in processing costs.

Incumbent banks will have to create a new way of working to deliver personalized customer interactions. They will need to progress from a small number of product-led campaigns which are led by the marketing team, to customer-led personalized conversations generated and curated by a cross-functional personalization team. Acting on the roadmap is the best way to bring the new way of working to life, with agile cross-functional teams working together on executing the program roadmap. Partnerships that complement existing offerings and technical capabilities will often be necessary and should be selected according to each bank's particular needs.

Incumbent banks increasingly need to shape their value propositions around solving problems for their customers, and shifting towards ecosystems is a promising step in that direction. First National Bank and Nedbank have been successful with this approach and have created an ecosystem of services that span beyond banking, including property and vehicle services, and a broad spectrum of convenience and lifestyle product partners in entertainment and travel. Standard Bank has done similar with its homeowner marketplace. This anticipation of needs is key to capturing and retaining customers before they go to market to seek the product or service from a competitor.

Conclusion

In the increasingly competitive retail banking space, incumbent banks need to find ways to regain their customers' love. By reimagining what is possible and leveraging their vast stores of customer data to engage with their customers in a new and more personalized way, they will be able to retain their privileged place in customers' financial journeys. Utilizing high-quality digital channels is key and increasingly demanded by customers. New customer-centric interaction models and revised business models that fit this new, bionic world will be required. There are certainly challenges to overcome, but with investment and a holistic transformation to ways of working and customer engagement, change is possible. To achieve all the resulting gains, persistence and decisive action across relevant capabilities will be critical. The future is undoubtedly bright for those banks that can successfully transform into this new role.

About the Authors

Frédéric Boutet has worked in the field of finance for over 20 years, both as a consultant and as a banking executive. At Boston Consulting Group, Frédéric works primarily within the Financial Institutions, Insurance, and Principal Investors & Private Equity (PIPE) practice areas. Within financial services, Frédéric has expertise in digital, data and analytics, large-scale transformations, cost cutting, growth strategy, and marketing and sales. At BCG, he has worked with multiple African, European, and global banking, and insurance clients.

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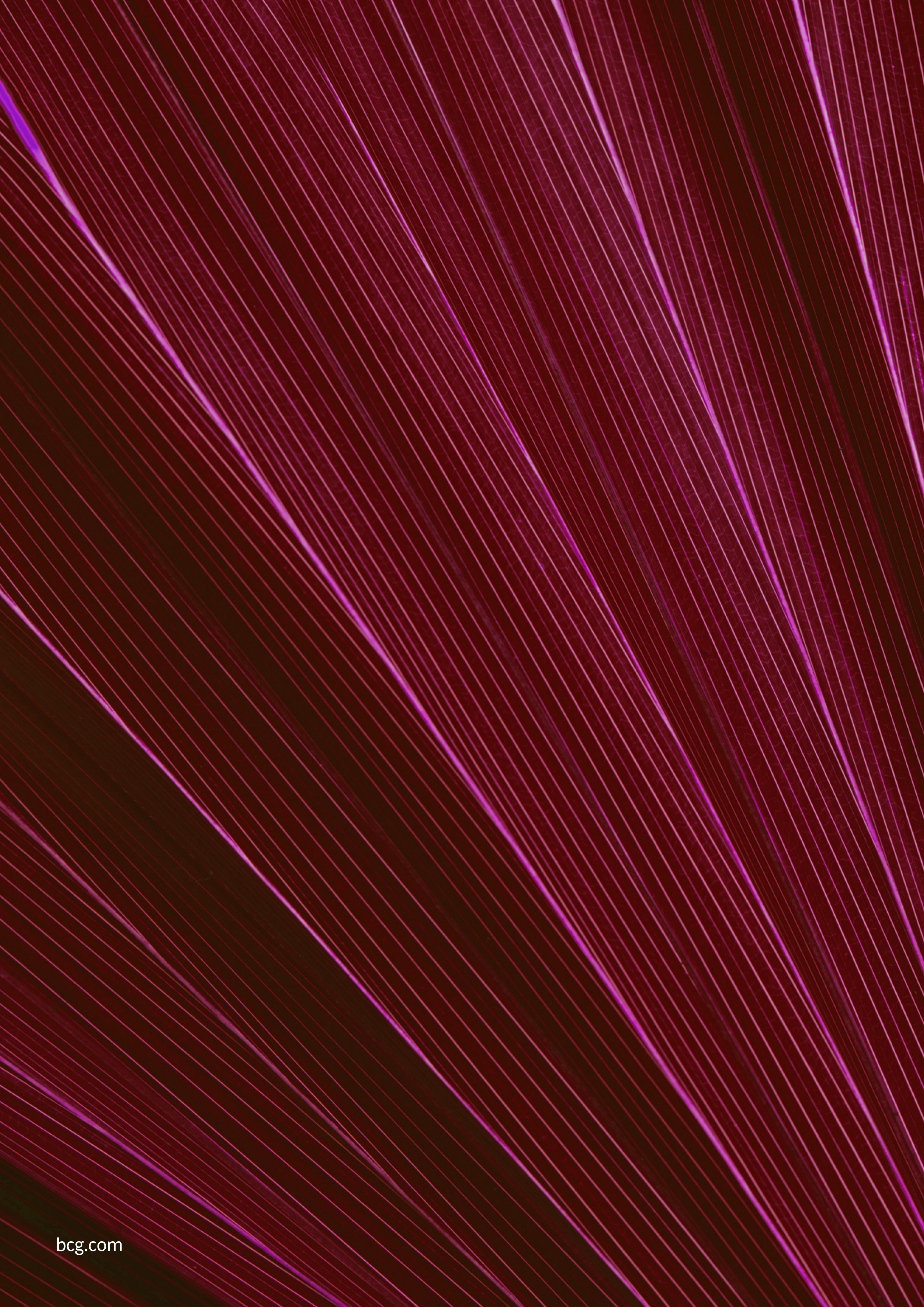
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