

Lateral thinking and agility are essential in a changing world

THE PARTICIPANTS



THE CHAIR:
Stephen Timewell,
editor-in-chief,
The Banker



Sandeep Chouhan, head of
global application delivery
services, Barclays, Global Retail
& Commercial Banking



Amit Dua,
head of sales, EMEA, Finacle,
Infosys Technologies



Michelle Price,
technology editor,
The Banker



George Gorshkov,
managing director,
retail business, VTB24



Deepak Varghese,
head of retail banking,
ICICI Bank



Eric Leenders, executive
director of retail banking,
British Bankers Association



Simon Carter,
director of business
systems strategy,
Co-operative Financial Services



In many parts of the world, the global economy is being driven as much by trade in information, ideas and services, as by trade in physical goods. Organisations that were able to achieve success and predominance through sheer productivity and massive scale are now fewer and far between. Increasingly, it is the ability to think laterally, to operate on an agile basis, to react to global trends quickly and, above all, to innovate that will determine the sustainability of an organisation in future.

In the Western retail banking community, these attributes have not always been forthcoming. Driven to a large extent by a service-weighted model, retail banking institutions have, by and large, delivered products and services to their customers with little regard for whether that product or service suits the immediate needs of that customer. Smaller, emerging players are starting to nibble at the banks' traditional revenue streams.

Meanwhile, the growing needs of a massive global unbanked population in emerging markets presents its own problems and opportunities for banks operating in those markets. The need for creative, cost-efficient, usable banking channels, products, services and operating models has never been greater.

The short-term prospect of a major global economic downturn, and the related impact on household expenditure, will also force the retail banking industry – particularly in the worst-hit Western markets – to think more dynamically when it comes to investing in and deploying new products and services.

These were the themes that were explored at The Banker's round table on the future of retail banking. The debate was sponsored by Finacle from Infosys but independently edited and written.



The changing global consumer

In the long view, it is vital to identify which forces are proving most powerful in driving change. This was the question that Stephen Timewell, editor-in-chief of The Banker put to the round table participants. Simon Carter, director of business systems strategy at Co-operative Financial Services, identified the consumer as the ultimate agent of innovation: "Innovation has to be driven by customer demand. If it isn't, frankly, the investment in it is going to be wasted."

Focusing on the customer and what Amit Dua, head of European operations at Infosys Technologies, identified as "increasing customer expectation" is fundamental in the battle to create services that are not only innovative, but also



WATCH NOW

Videos of the panellists in debate are available online. Watch the debate or individual chapters – visit thebanker.com/media

useful and, in turn, well-adopted and profitable.

In this regard, the banking industry could learn a great deal from retailers in other markets, Mr Carter said. The successful deployment of powerful customer relationship management technologies has allowed major high-street organisations to segment their customer bases into multiple demographic profiles, and develop an in-depth understanding of each segment's needs and expectations.

Ideally, the banking industry should aim "to have every single consumer

representing a single person segment”, said George Gorshkov, managing director, retail business at Russian retail bank VTB24.

Michelle Price, *The Banker’s* technology editor, said that an increasingly detailed view of the customer was driving the personalisation of a vast range of consumer products and services in other retail markets. “If you look at the way consumer products have developed, taking for example the iPod, it’s increasingly about allowing the user to enjoy a unique, personalised experience. The same should apply to financial services.”

Having identified each customer, the next logical challenge would be to offer each customer a personalised bundle of products and services, she said.

The needs of customers are ever-changing, however, determined by a range of demographic forces that are constantly in flux: social mobility, population migration, population growth, the rise of globalisation, and increasingly ethical and religious preferences. Islamic banking is a key example of how the religious needs of one demographic group are increasingly being reflected in the products and services of global >>

THE ISSUES

- > The changing global consumer
- > The role of technology
- > Embedding innovation in culture
- > The future of innovation
- > The new operating model

> THE KEY ISSUE

The new operating model

Embedding innovation in the culture of the organisation will not, ultimately, be the conclusive factor where realising innovation is concerned. More important is understanding how banks can develop a sustainable operating model, said Mr Timewell. That means determining “who is going to pay”.

The UK is in a difficult predicament in this regard, said Mr Leenders. During the past 25 years, disadvantageous cost-structures have become well established. In general, “there is an expectation among consumers that banking is fee-free”, he said. The current account is just one example of this phenomenon – a service for which consumers pay a fee in other markets, including the US.

Online banking, too, is a convenience for which customers do not pay in the UK, and through which they can often derive better deals on products such as savings bonds. “To move away from a fee-free model is a difficult move,” said Mr Leenders. Some niches have been identified, for which consumers are willing to pay a fee. “But to start to fundamentally attack the nub of the problem will be a long, hard-fought campaign.”

To some extent, this problem is the product of commoditisation often seen in mature commercial markets. In emerging markets, where the vast majority of banking services still hold what would be regarded as an

added-value or novelty status in established markets, consumers are happy to pay a charge. But there is a “double-edged sword” for emerging markets banks, observed Mr Varghese: to be able to offer these services, they have to operate at a fifth of the cost of their counterparts in mature markets; but in achieving a low-cost operating model, they are at a distinct advantage competitively.

ICICI, for example, was able to follow non-resident Indians into developed markets through its online banking offering. “In doing so, you are bringing that cost advantage to a developed market,” said Mr Varghese.

From a Western-based bank’s perspective, the ICICIs of the industry “have really got the world of banking worried”, said Mr Chouhan. If ICICI is now playing in developed markets, with an operating capability that allows them to drive down cost, then the conclusion seems inevitable, he said. “What will they do with that cost? With that operating cost, they will price their products in a way that will wipe everybody out.”

In established markets, where the majority of consumers’ needs are being met through sophisticated technology infrastructures, innovation must become a network concept, said Ms Price. This means building out collaborations with non-banking players and delivering products and services through

channels that the banks do not own: optimising the established commercial infrastructures to reduce operating costs. “The presumption is always that the bank will own and control the channel. But, in future, banks will have to integrate their services with channels that are not under their full control,” she said.

This model has already been successfully deployed by some of the world’s most successful financial organisations, American Express being a key example, said Mr Gorshkov. Among the most profitable financial services organisations globally, American Express has conquered what he called the “invisible concierge” model. “It’s a service that’s embedded in your life; you don’t really look at American Express as a payment instrument: you use it to book a restaurant, to book hotels and cars. Although the UK is a fee-free banking space, you look at the American Express British Airways co-branded card and the APR is 36% in pounds. Yet it’s one of the most successful co-brand projects in the world.”

The card is a key study, he said, because consumers are prepared to pay for a product that costs three to four times more than its average competitor because of the high level of convenience it offers. It is also a model in which the bank deploys, but does not own, multiple distribution channels. This, he concluded, is the “new paradigm” for banking services in established markets.

“THE WORLD IS SHRINKING. CUSTOMERS ARE DEMANDING SERVICES ACROSS GEOGRAPHIES”

retail banks, said Mr Timewell. In other regional geographies, such as Japan and Germany, ageing populations are demanding products specific to retirement, including high-yield savings plans and a vast range of health insurances.

Other factors also affect customer needs. Banks that target younger demographics – for example, Spanish banks that are hoping to capture the immigrant Hispanic population in the US market – will need to adapt to their customers’ changing requirements. Today, such customers might only need to make remittances. In future, as their earning power grows, they may need a car loan, a mortgage or a savings product. “As long as the bank can tap that entire life cycle, the bank is going to make money,” said Mr Dua.

And it would be a mistake to assume that the needs of customers will be confined to the geographies in which they are located. “The world is shrinking,” said Sandeep Chouhan, head of global application delivery services, Barclays, Global Retail & Commercial Banking. “Customers are demanding services across geographies. They not only want to be able to move money, but to access products in various markets.”

The role of technology

Increasingly, established banking players will have to compete against a broader and more diverse set of players in a broader and more diverse set of channels, and in a range of global markets. Here, the use of innovative technology will be critical.

To a large extent, changes in customer expectations have themselves

been driven by the ubiquity of technology, said Mr Dua. Many of these technologies have proven vitally important in rolling out and supporting new, inventive banking delivery channels – a key example being mobile banking and remittances. But in turn, technology has also been disruptive, he said. The emergence of the comparison engine, for example, had served to depress profit margins on products and to erode customer loyalty.

Meanwhile, low-cost online platforms and free Web 2.0 technologies have dramatically reduced the barriers to entry. “We have seen the disruptive influence of newcomers to the UK market, who enter with very low cost-income ratios and compete very well in certain niche markets,” said Mr Dua. Many of those newcomers include non-banking players boasting major brands, such as supermarket giants Tesco and Wal-Mart. “More than ever before, customers are expecting and using a variety of technologies to bank,” he said. Like their emerging competitors, established banking players will have to continue to use technology as the underlying platform through which to achieve differentiation.

But banks should not pursue technology for its own sake, participants agreed. The importance of deploying technology-driven products and services in the right way is vital. “We have seen, at points in time, excellent technology products. But the front line did not know how to use them for the best benefit of the customer,” said Deepak Varghese, head of retail banking at ICICI Bank. “The front line has to be as aware of technology and contribute to the development jointly.”

More importantly, banks must ensure the “structural integrity” of the technology infrastructures by which they are delivering new products and services, said Eric Leenders, executive director of retail banking at the British Bankers Association. “I think it is very important while talking of innovation to make sure that the underpinnings are absolutely solid. Otherwise, I think we’re adopting a very high risk strategy with technologies.”

Participants also agreed that the vendor community is not serving the space as well as it could. In terms of its intuitive ease of use and flexibility, consumer technology – to which banking customers are exposed daily in other

areas of their lives – has far outstripped the technologies being delivered to the enterprise space, said Mr Chouhan. But the vast majority of consumer technology is not yet industrial grade, he added. There is a huge gap between the innovative technologies seen in the consumer realm, and what the traditional software community and systems integrators can offer the banks as a complete package.

“They are bringing reasonable ‘cookie cutter’ solutions to market, and then banks like us are spending an arm and a leg to customise it,” said Mr Chouhan. “Everybody sells the car in parts: nobody sells you the car.” This is proving a major barrier to innovation, he said. “Vendors need to be collaborating much more than they do today,” he added.

Mr Dua conceded that, in many respects, the two spaces are “out of synch”. It is incumbent upon the traditional vendor community to keep in touch with technology developments emerging in the consumer realm, particularly those platforms associated with Web 2.0 technologies, he said. “For all you know, the best ideas can come from that space. There is a lot more the vendors could do to improve the situation,” he added.

Banks that “push the vendor to bring you what you want in your marketplace are going to be there tomorrow,” said Mr Chouhan.

Embedding innovation in culture

Understanding how innovation can be embedded in the fabric of the organisation is a key issue, said Mr Varghese. Because market developments emerge and change so rapidly, it is not enough that organisations create innovative products or services he said: an innovative culture must become ingrained within the processes and organisational structures that underpin those products and services. “Organisations need to look at how they can embed innovation across business units, from risk to compliance to operations.”

ICICI is a good case in point, Mr Timewell pointed out. The bank is one of few – if not the only – banks in the world in which the CEO also assumes responsibility for IT operations. “His understanding of what he could do with the technology was critical to how he managed to change the model,” said Mr Timewell. In the vast majority of cases,

it requires forceful leadership of this kind to permeate the organisational structure with a chosen cultural value.

Mr Gorshkov found this to be the case when conducting his own research. "If you look at corporations like Microsoft or Apple, the innovative drive comes from someone you can identify: Bill Gates or Steve Jobs, or Richard Branson. These people become flagships of innovation," he said.

Mr Carter agreed that culture will play a major role in the pursuit of innovation, adding that this role would be more important even than that of technology. This was the experience of the Co-operative Bank which, in the early 1990s, underwent a rebranding exercise, the centre of which was the bank's now well-recognised ethical positioning. "Suddenly, the Co-operative Bank meant something different that became a launchpad for innovation," said Mr Carter.

The bank was among the first in the industry to offer an online banking service. "We had legacy in terms of technology, but people found ways around that. Innovation is very much a mindset: it has to become the blood of the organisation," said Mr Carter.

➤ The future of innovation

To what extent the Western retail banking community will go on to embrace this model remains to be seen. In the UK, argued Mr Carter, the most successful banks will be those that develop an in-depth understanding of their customers. "Consumers don't think they're a demographic: they just think 'I'm me'." Banks have to create services and products that are relevant to the individual if they want to fully differentiate their brand, he said. "At the moment there is not a huge brand differentiation in most financial services organisations."

In turn, those brands are likely to produce and own less themselves and instead source more from other third parties, he said.

For Mr Gorshkov, however, a utility model is preferable. Much like water or electricity suppliers, banks should become invisible, but their service ubiquitous, he said. "In 20 years' time, I don't see the banks at all. When I need water today, I open the tap and water flows and I don't have to apply to the water company to adjust the temperature of the water. I want to be able to



operate my life as freely as I can without thinking about the bank," he said

Mr Chouhan suggested that the speed of service fulfilment would become a key differentiator. "Banks will differentiate themselves on the one-minute loan and the one-minute deposit, and the instant gratification of fulfilment if you may," he said.

Mr Varghese agreed that the banking services that customers receive would in time become entirely customised. "Your bank is going to become like iGoogle," he said. But to achieve this model for each customer, banks will have to start using resources as incremental, rather than fixed costs. "This means having the ability to draw on your resources when you need them, across a global pool, but without paying fixed costs for having an idle engine," he said.

Achieving economies of scale globally, particularly where technology infrastructure is concerned, will also be critical, Mr Dua pointed out. Banks have to keep standardising and rationalising their infrastructures continuously, he said.

Meanwhile, in emerging markets, banks will be forced to undergo major infrastructure roll outs to reach more than 500 million people who are forecast to move from rural communities into conurbations and aggregated societies, said Mr Varghese. "It will therefore force banks to innovate, and legacy embedment will have to change. Technology is going to play a major role, but the key is what do banks ask of technology?" **TB**

“INNOVATION IS A MINDSET: IT HAS TO BECOME THE BLOOD OF THE ORGANISATION”

Sponsored by

Finacle
from
Infosys