ENVISIONING THE FUTURE - REALITIES AND MYTHS OF FUTURE BANKING

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The rapidly changing banking landscape has prompted a greater interest in understanding the changing dynamics of the present banking needs. This could be identified as an effort to retool their business model and thereby win over this very dynamism. The good news is that almost all banks except a few have successfully navigated the choppy water thus far. However, the Banks still have a long to do list or need to do their homework when handling these dynamics. This article is an attempt to elaborate on the business model which would help reshaping the future banking scene. In compiling this article several megatrends which appear to play key roles in the business model have been taken into consideration.

In brief, the business model maps out the general business strategy of a bank. Thus banks often review their strategies substantially and benchmark with their peers and the changing market conditions. The Business model is a combination of specific business lines i.e. products and services in which a financial institution is mainly engaged and help employees and customers to understand the Company's specialization in business. Accordingly, the Management can identify the applicable strategies in specific business models to compete in the market. Nevertheless, a business model creates concentrations in business which may not be healthy if pursued without a revision for a long period. Concentration risks may cause business bubbles and sustainability problems. Therefore, revision and rebranding of a sustainable model is important specifically in this digital attackers' era.

The Central Bank has categorized Sri Lankan banks into three groups based on their assets base, namely above 500b as large, between 200 - 500b as medium and below 200b as small banks according to which there are 6 large, 5 medium and 21 small banks operating in the Island. It is undeniable that all these banks have to face some sort of challenges including the following

i) to deal with a challenging macro environment
ii) to compete for the same slightly over sophisticated 21 mn customers
iii) to deal with technological changes specially, digitalization
iv) to deal with future possible threats of fin techs ,who are ready to attack banks on specific offering verticals
v) to deal with increasing regulations that include Basel III capital requirement, the highest demand with regard to the scope and quality of risk management.

vi) to deal with geo political risks
vii) to deal with millennial workforce

Combination of the above factors is leading to the development of a new business model. It is clear that common developments are taking place in almost all Banks in Sri Lanka, with the launch of digital banking, alternative customer touch points, various kinds of payment systems, core factors etc. But these developments are taking place in different spread levels among these 32 licensed banks. At present, banking sector generates a profit of Rs. 98 bn (after tax) as at end September 2017. However, whether a bank's respective business model is any more viable to generate sustainable returns over the years ahead is a question.

Digital transformation

Just as the other industries, digital transformation is completely changing the banking game as well. In today's point of view a digital experience is an imperative rather than a luxury for banking institutions. So the digital transformation is not just the buzzword today; it is an integral part of a bank's future success. Therefore, the digitalization is the key parameter and the foundation of the new business model for the Bank.

Financial Institutions are no strangers to change. Banking institutions are flooded with the opportunities to add new technology. In order to launch a truly digitally fit business model a bank should begin with a detailed road map. This process can be difficult especially when considering the prioritization, difficulties and potentially dealing with the legacy system.

Some of the new trends and practices adopted by global banks which need to be understood and considered under the Digital Darwinism are discussed below.

As the customers increasingly rely on their personal electronic devices to meet their banking needs remotely, they are naturally relying less and less on the traditional brick and mortar branch. Of course, much 21st century convenience has been engendered through various digital solutions which the financial institutions are making available for their customers. The downside, however, is the inevitable deterioration of personal relationships that the customer has historically forged with their banks, due to the fact that the face to face customer interactions have, in some cases, all but disappeared.

Today, the banks are working on a number of initiatives to remedy this issue. The banks are now turning to another digital channel, video banking, to help nurture their key relationships with their many small business customers, and bring back some of those all-important face to face interactions albeit that they occur online as opposed to in the flesh. The banks can make use of 3rd party integrated video collaboration to offer immersive, remote video chat to small business customers across the island to converse face to face with their bankers from anywhere and practically using any device – be it a smart phone, tablet or desktop computer. Video banking has become increasingly important for today's digital savvy millennial. A high quality reliable video banking service is an exceptional addition to a bank's tailored approach to servicing its customers, where 24/7 access to advice and services is strengthening customer relationships. The video tool could also be used to perform an advisory role for the customers' wealth management and to educate the customer to abide with Customer Charter introduced by the Central Bank Directions of 2008.

Today, providing an omnichannel banking experience is fast becoming an imperative for financial institutions to be abreast with the swiftly changing technology. As more and more customers chose to be digital as they go to channel for everyday transactions, banks are challenged to ensure that they are delivering across multiple touch points - branches, desktops, phone lines, mobile indeed., A recent research carried out by JD power (2017, US Retail Banking Satisfaction Survey) reveals that today's customers more than ever are using mobile banking to a 49% of millennial, 31% of Gen X and 16% of boomers and that some 79% overall are regularly engaged with a bank's website. However, crucial to the omnichannel experience is the promise of "seamlessness". Not only do the customers expect to be able to choose between numerous channels when doing business with their bank, but they also expect to have the ability to move between them with absolute ease and agility. But standing in the way of such "seamless" transitions is security. Of course, customers expect the financial institutions they deal with to provide the most stringent privacy and security guarantees across every communication and every transaction that they make. But in the world of onmichannel experiences, if a customer is continuously having to authenticate him/herself when switching between channels, the notion of "seamlessness" goes out of the window. Therefore, banks are compelled to provide solutions to this problem by developing platform connects applications via API (Application Programme Interfaces) to enable multiple biometric authentications – eye, voice, finger print and face recognition all in one place.

The evolution of the Internet of Things (IoT) and the development of other new capabilities have presented many opportunities for financial services companies to develop services that can improve the global and multichannel experience of the customers. For example, the banks have started using robots in branches to enhance the customer experience incorporating the technological advancements with a different kind of a personal touch. Robots can serve customers using state–of-the-art multi-lingual speech and voice/face recognition technologies, accumulate customer interaction data to analyze and discover customer needs and improve branch security by monitoring customers with facial recognition and behavioral analytics. In general the customer response had been positive, with some segments even preferring this delivery over other traditional approaches.

Fintech Collaboration

Since 2016, there has been a significant move from banks fearing startups who wanted to disrupt banks. Mobile apps play today an important role eg. Apple pay is used for 90% of mobile transactions in USA and is now able to be used at half of all American retail locations. In 2016, more than any other economy, Chinese consumers have spent $ 5.5 trillion through their mobile apps. Many predict that China will be the first major economy to be completely cashless.

They always make it a point to choose a mobile payment system and most Chinese citizens prefer Ali Pay and they have recently started to expand its footprint globally. Today Ali Pay monitors every transaction from its 450 million users, in real time with artificial intelligence monitors; constantly searching for potentially fraudulent transactions. When compared to VISA and Master Cards, they handle over 60 billion transactions per year and on average close to 2000 transactions per second. With the use of Ali Pay's new machine learning and super intelligence structure, it is possible to process 250,000 transactions per second and 100 billion transactions per day. There is no payment or bank thinking in Ali Pay and just a technology firm that wants to enable the best customer experience.

Ali Pay has signed deals with Ingenico and Wirecard to allow their customers to use the mobile app in Europe, in USA with First data and big scramble to acquire Money Gram, the global remittance service provider.

The financial money market fund called Yu'eBao (Hidden Treasurer) is the biggest money market fund in the world, exceeding $ 165 bn of assets under management, in February, 2017, which is more than JP Morgan's US Government money market fund of $150.

Ali Pay has also initiated Ant Forest, which is all about making a better planet. Ant Forest is a game, but it is a part of an Ali Pay Mobile Wallet. The idea is that every time a customer pays, the customer can offset his carbon emission in the app and move points towards the customer goal of planting a tree. The results are impressive. In April 2017, there were over 220 million users. These users had already contributed to emission reduction of 5000 tons per day. It has further planted a total of 8.45 million trees, which reduces carbon emission by another 2500 tons per day. This is a CSR activity that banks also can initiate.

The bank has the customers; capital and credentials while Fin tech has the ideas, vision and passion and as such the best thing is to combine the two and form a strategic alliance through which the banks can get a better outcome than struggling with their own agendas.

Distributed Ledger Technology (DLT) could reshape many global payment issues namely the time zone differences, cut off times and other complexities add to delays. The banks have long sought the ultimate efficiency of full inter-operability for global payments of member companies to fully mobilize their cash flows. DLT could be the catalyst to enable this leap. VISA took 60 years to rollout three billion cards and equip 44 million merchants to make card payments. In the next 5 years there will be 30 billion ways to pay and 440 million places to buy. At present in Sri Lanka approximately 20 million VISA cards, 45,000 POS devices are operating island-wide with Rs. 300 bn worth transactions.

Gartner has made a series of predictions beyond 2018. By the end of 2020, the Banking industry will derive $ 1 bn in business value from the use of blockchain-based crypto currencies. Gartner estimates that the current combined value of crypto currencies in circulation worldwide is $ 155 bn (as of October 2017) and this value has been increasing as tokens continue to proliferate and market interest grows. Crypto currencies will represent more than half of worldwide block chain global business value-add through year-end 2023. In the digital economy, physical money is soon to become a thing of the past. Crypto currency with the knowledge that digital payments are already so prevalent in countries and it is advisable to begin setting up crypto infrastructure now itself.

Another fact which would reshape or shake the industry is the rise of chatbots and conversational interfaces as new interaction paradigms. They are not just a possible solution to the lower customer service costs but also an effective tool to engage with customers in a completely new way, being exactly where they want the banks to be.

With the development of IT, it is needless to say that banks are also well equipped with the adequate cyber security. According to the EY's Global Information Security Survey, the majority of the businessmen are still unprepared for sophisticated cyber-attacks. The Survey has also showed that 56% of the organizations are unlikely to deal with sophisticated cyber-attacks and 74% say their cyber security measure only to partially meet their needs.

Digitalization demands a fundamental rethinking of structure, products/services, management and operations. It is completely a different business world. There is more change in the next few years than in the last several years and dived into how the IOT or, the intelligence of things will change everything.

Mckinsey research published in September 2016 found that the widespread adoption and use of digital finance could increase the GDPs of all emerging economies by 6% or total of $ 3.7 trillion by 2025.

Regulatory Aspect

As a heavily regulated industry, regulation also plays a vital role in determining banking business models. Regulatory reforms are fundamentally changing the landscape of the banking industry. These multiple new regulations have led to intended and unintended consequences which modify the traditional functions of banking institutions. Resultantly, the banks need to refresh their strategies on how they respond to regulations and how they carry on their business in this changing legal environment that could be fundamentally more constraining.

The future election results may, over time, reshape the banking industry's regulatory landscape. Key regulatory areas, such as consumer protection, financial crimes regulations, income tax, capital and liquidity requirements has apparently been experiencing uncertainty. And time will tell how these events may impact the banking industry. The banks may need to be vigilant and pay further attention to regulatory changes as they unfold as the industry's regulatory trajectory may shift.

At present the Central Bank is requesting all banks to provide suggestions/proposals to incorporate in to the new Banking Act which will be executed as an amendment to the existing Act.

We also need to keep an eye on the proposed amendments to the existing scope of certain regulations not only in Sri Lanka but also in the developed countries like USA and in Europe which definitely has a spiral effect. There may be further capital reform initiatives, which complicate the banks' efforts to pursue an appropriate business strategy. Further, new regulations of increasing capital under BASAL III and proposed leverage ratio are reinforcing the robustness of banking industry stability. These regulations may provide an opportunity as well as a threat to the fraternity which banks need to address.

Since cyber-crimes continue to grow at an alarming rate and the entire financial services industry is at a risk due to its high levels of interconnectedness the amounts of loss are growing exponentially and the customers are demanding more openness and access. Based on the cyber threat real time map, Sri Lanka has been identified as the world's 34th most attacked country. Microsoft Security Intelligence Report has revealed an increase in the number of security incidents reported in Sri Lanka under malicious software in 2016. Therefore, regulators are getting more involved in and focusing on cyber risks and request to implement more and more risk management initiatives, e.g.: a written enterprise wide cyber risk management strategy, integration of an internal and external dependency strategy into the overall strategic risk management plan etc. The Central Bank by their Road Map – 2017 has also stressed the enhancement of the three lines of defense model.

The banks continue to increase a large part of their discretionary budget to keep up with these escalating requirements. A strong and well-functioning banking system is a vital cog in the banking sector and in this scenario, banks' Consolidation program, which has been initiated during the tenure of the previous government and halted during the early stage of the new regime, has resumed its journey. This may be a future challenge to the banking sector. There is a need for greater certainty around the regulatory agenda and for policy to focus on the role of banking as a positive contribution to the economic growth.

Millennial Employee and Customer

Millennial is becoming an increasingly important demographic segment both in terms of customers and employees for the banking industry. Approximately 7 million Millennial live in Sri Lanka today. They will be defined by their ability to create an internal culture that weds dynamism to best practice. They will be defined by their ability to deliver new fit-for-purpose business model.

Banks are competing forcibly for the best available workers and for the talent that will replace the retiring Boomer generation in the coming few years. They are expected to make up an approximately 50% of the workforce by 2020. Finding skilled, experienced and responsible employees is a challenge for any industry, therefore getting the best of these millennial workers is critical to the future of the Bank.

Key diversity challenge facing the banks is that there are multiple generations working together, millenniums (1980 – 2000) Gen X (1964 – 1980) and baby boomers (1946 – 1964) and they show different pros and cons at works culture. Gen Y is believed to be the most tech savvy and enthusiastic about their jobs. Gen X workers considered to be the most effective managers and Boomers are considered hard workers rather than smart workers. The job of HR in this scenario is very tough and may be able to get the maximum of all types of generations in a harmonized manner amidst this rapidly changing environment.

Millennial workforce has a strong desire to be a part of the change. As a collective body they must take action to transform the existing challenges into opportunities, push boundaries and rethink current systems by exploring new models of growth based on human dimensions, cultural identities and a sense of purpose. The positive or negative impacts of decisions made today will either be enjoyed or suffered by the generations of tomorrow. Hence it is highly critical that young people play an active role in decision making process on issues that would affect them in the future. Dynamic in their thinking and action oriented, young people need to take on more leadership positions. Since millennial are willing to obtain constant feedback, this character trait could also be used by the banks to obtain more innovative ideas for doing business in different manners. According to the Forbes Magazine, engaging people well is becoming one of the biggest competitive differentiators. In this backdrop, the writer proposes to include these talented young blood to all important banks' internal committees like, ALCO, Credit, Product development etc.

However, most of the Bank employees are often highly specialized and focused only on their specific business areas. Employees need to change from silo mentality and need to be the holistic employee who will be able to cater or find solutions to any business segment problems. In this connection, Gartner, also predicts that by 2021, 40% of IT staff will be versatile, holding multiple roles, most of business, rather than technology related.

With the development skills of their IT, they may also be smart enough to get involved in financial frauds. Therefore, the internal controls need to be in place to ensure such mistakes do not to happen at all.

Millennial is viewed as "Managing performance and career opportunities for the most engagement drivers". Creating engagement strategies is one of the management's big goals. Millennial tends to be uncomfortable with rigid corporate structures and turned off by information silos. Millennial wants their work to have a purpose, to contribute something to the world and they want to be proud of their employers. The employer brand, the reputation and corporate values play an important role. Based on the hopes and expectations of the millennial the banks and HR Leaders need to revise their current strategies accordingly.

Another important factor to be considered in this millennial workforce is the women segment. While they have made significant strides in education, women's labor force participation remains low, but in the banking sector in Sri Lanka over 55,000 are working at present and women also represent equal proportion. However, this proportion may impact the future once they enter into family life.

According to the study by the McKinsey Global Institute estimates that Global GDP will increase by 26% by 2025, adding $ 12 trillion, if the gender gaps in economic participation were closed. So the tackling childcare can be a major contributory factor in closing these gaps. The Next Generation Work Place in 2017 Conference held in Sydney in mid-July highlighted the importance of employee health and wellness in the work place.

Retail banking is likely to experience a dramatic change when they are with tech savvy millennial customers. The CX (customer experience) has changed, traditional banking customers have transformed into millennial digital customers. They pursue their own independent search with high expectations of their banking experience and they specially want banking products and services to be personalized for their own needs. The bankers should rethink how to deal with their millennial customers.

Millennial customers now use social media or smart phone internet to evaluate product benefits and pricing, etc. without the support of sales people. Therefore their new purchasing process is making a profound impact on how the banks are required to interact with them. Designing great customer experiences is not just about the customer experience optimization. It is about the entire UX (user experience) and how banks can offer their services accordingly. Millennial workforce needs to discover millennial customer micro movements that a customer has when they are engaging with your brand, because they are not any more loyal and bank switching can take place. Therefore, delivering a valuable content and strong UX will be vital for growth, engagement and conversion.

External Driving Forces – Government and Geopolitical

There are external driving forces that demands the banks to integrate sustainability within their day to day business and corporate policies. These are driving forces derived not only from the need to minimize exposure to risk but also the opportunities to be gained. In this respect, Government vision and policies are major driving forces for banks. It is a duty of the banks to react and support Government attempts and to understand its economic dynamics.

Numerous potential economic growth determinants have been identified by the unity Government under its new vision of 2025. But of the many ambitions and challenging goals, the writer wishes to emphasize and identify the challenging role of the banks in receiving Foreign Direct Investment to an extent of USD 5 billion per annum. In order to attract more FDIs it is needless to say that country should to improve its global rankings, in some leading indexes. The Easy of Doing business and Global Competitiveness index are two major contributory indexes for the same. Access to Credit and Finance market development are two determinants or sub-indexes of the above indexes in which the banks could play a pivotal role by achieving Government objectives. The Government has also indicated that they will soon introduce several laws to improve the ease of doing business. There is no short term silver bullet solutions to this issue.

As we all know, Sri Lanka is a nation of geopolitical importance despite its relatively small size. Strategically positioned near key maritime sea lanes that transit the Indian Ocean and link Asia with Europe and Africa, more than 60,000 ships carrying 66% of the World's oil and 50% of the World's container shipments transit the sea lanes near Sri Lanka each year.

With the growing strategic competition of India and China, Sri Lanka has become pivotal in balancing their strategic interest in a challenging environment. Free Trade Agreements (FTA) with China, India, Singapore and with Japan and Malaysia, GSP + with EU and GSP with US boost our export growth, a Foreign Direct Investment and job opportunities. All these facilitate the banks to look at their business in a more positive note. Savings investment gap presently experienced by the country to be bridged by the domestic savings component by introducing innovative savings instruments.

Conclusion

The Banks need to capitalize on the potential talent of its millennial work force to convert classical economic resources into more monestisable value for the future. The Banks need talent to win the war of its future growth and capability arbitrage.

Every bank should develop and build learning staff, resourcing it with innovative technologies, agility backed by data analytics, value creation through positive governance; this is the only real long term sustainable differentiator in the market which determines the banks' sustainable economic growth and stability.

This article has made an attempt to understand constraints, realities, myths and identifying appropriate strategies to redraw the bank's business model which provides an insight into building a strong bank.