Banking in a Digital World

Insights from leading retail banks worldwide on the state of play and expected challenges in the digital banking journey
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Preface

Digital banking is not just more hype about the next big thing in the market. It is a necessary part of every bank’s agenda as a way to overcome outdated approaches and mismanaged client relationships. Banks around the world are actively pushing digital topics both internally and externally.

However, the steps taken so far—a combination of testing new offerings and following other market leaders—are just the beginning. True transformation will require deep, extensive change and letting go of old habits such as offering complex products and requiring clients to go to branches. It will also mean cleaning up legacy processes and technologies within the organization. Archaic structures will need to be dismantled to create a new, nurturing environment. The journey could be painful, but forward-thinking players will start now.

The clock is ticking. For some regions, the environment for digital banking is more advanced, thanks to regional banking capabilities, domestic customer demands, external market dynamics, and regulations. Although the ideal timing will depend on the regional atmosphere, banks all over the world are going digital, and their approaches are fascinating.

In this joint research between Efma and A.T. Kearney, we look behind the scenes to see what banks in other countries are doing, and we shed light on the next steps in the digital banking journey.

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Executive Summary

Across the globe, banks are exploring ways to convert to a more digital business model. So far, the changes have not been too disruptive, despite aggressive new offerings from non-banks. Besides gradually reducing paper-based interactions, the primary focus has been on enhancing the product suite with value-added services and achieving an integrated channel experience.

Thus, the focus has clearly been on the outside—the customer-facing side. Very few players have fundamentally changed their internal organizations or governance principles. Most customers still belong to branches, and in the back office the preparation for being the central customer interaction coordinator has been timid. Consolidated IT systems have helped reduce cost but do not cater to fast time-to-market and processing.

In addition to this mismatch for banks, the pace of change is increasing: New technology-savvy companies are flooding the market with innovative offers for financial services, customers are becoming more confident in using the full range of e-commerce offerings, and even regulators are reshaping long-established procedures to adapt to new concepts. Some regions are more advanced than others, and the timing of change is hard to predict, but banks are well advised in already preparing today.

Digitization will become more disruptive as value chains break apart, especially around customer interaction, product configuration and transaction processing. Moving forward will require flexible processes, new revenue models armed with new products and services, and sweeping cultural changes—all in sync with the regional environment. Our Digital Banking Readiness Index (DiBRix) can be used to guide this journey.
The Digital Banking Journey

Digital banking means more than just going paperless. Leading players are offering a new and improved customer experience and delivering faster and more efficient services.

**Smart, convenient, demanded—but still missing**

Digital banking has been around for years, with many experts calling it the cure for the shattered banking industry after the recent financial crisis. And they are probably right.

However, banks are not known for being fast movers. Customers are still waiting for this new banking experience, touted as a revolutionary transformation that will bring many new features, including anytime and anywhere banking, ultra-fast response times, and omnipresent advisors. So why don’t banks just pick up the pace? Because it requires more fundamental changes than expected at first sight.

The industry has been in a comfortable position for decades with low customer turnover, almost no regional competition, good personal relationships and trust as selling points, and not much intervention from regulators. Staying ahead of the curve was easy, and there was no pressure to change.

Now, new competitors from adjacent industries and financial technology startups are flooding the market with innovative, technology-driven deviations from the traditional banking model. And to add insult to injury, customers’ attitudes have fundamentally changed. They are making decisions much faster and have access to a plethora of offers, leaving financial institutions struggling for customer loyalty.

The challenges in this fast-moving, demanding digital world are tough. The issue is not finding new digital solutions; the issue is the industry’s long-standing history of not keepiing in shape. The best running shoes will not make up for poor fitness, and banks are just warming up for the road ahead.

**The digital banking promise**

Ideally, digital banking combines the benefits of two worlds: a new customer experience on the outside and an efficient, effective operating model on the inside—both enabled by digitization and the underlying technologies, processes, and structures (see figure 1).

On the outside, customers benefit from fair prices with increased transparency and comparability. Banks meet their needs with immediate, high-quality interactions, and transactions are performed quickly and securely. Purchasing a product no longer requires 14 days. Customers are proactively informed about a rich spectrum of personalized products and services, including financial advice, new opportunities, and peer

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**Figure 1**

Digital banking offers the best of two worlds

- **New customer experience**
  - Immediate, high-quality interaction
  - Fast and secure processing
  - Rich spectrum of products and services
- **Efficient and effective operating model**
  - Lean channel and organization structures
  - Streamlined governance and agile culture
  - Integrated IT and infrastructure
  - Enhanced revenue model

Source: A.T. Kearney analysis
comparisons. Overall, customers enjoy the banking experience, and they are happy to hear from their bank (or non-bank).

Making all of this possible will require support from the inside. The underlying operating model will need reshaping, with lean channel and organization structures in place to allow for fast processing. Decision and governance processes will need to be streamlined, with a new more-agile culture that has the right spirit to support a superior customer experience. An integrated IT infrastructure will be needed to meet all requirements, with fast computing to allow for super-fast processing. Last but not least, digital banking will change the way revenue is generated. As customer centricity becomes more important, deep customer insights will open up new sources of revenue, such as third-party advertising and customers paying for value-added services.

Banks on the Move

Banks are cautiously approaching these new challenges. While digitization is making internal processes more efficient, it is only slightly enhancing the customer offering with value-added services such as wallet solutions, personal finance management tools, and an omni-channel experience. Few solutions on the market are fully mature.

Only small steps so far: Enhancing products and services

The first steps on the digital banking journey have been primarily focused on adding to the existing offering using new, technology-enabled services to increase the convenience and value for customers. The most prominent examples are mobile apps, e-wallet solutions, and personal finance management (PFM) tools (see figure 2). In particular, mobile banking and PFM are well received by consumers, with download rates reaching 60 percent of the customer base in most regions. For example, on the mobile banking front, USAA, a U.S.-based banking and insurance

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**Figure 2**

*Mobile apps are leading the way for digital banking*

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Source: A.T. Kearney and Efma global retail banking study
provider, recently released an app with a Siri-like virtual mobile assistant, which allows customers to use voice commands to navigate and complete more than 200 actions from their smartphones. In Spain, CaixaBank offers a bill-management PFM service called ReciBox. Compatible with computers, tablets, and mobile devices, the free service helps customers organize their bills, and if there is an unusually large bill or insufficient funds, ReciBox will warn customers via text message or email before funds are deducted from their accounts. However, few banks offer more advanced PFM tools, with functions such as peer comparisons, automated product recommendations, and predictive capabilities.

Other solutions such as artificial intelligence, video and chat functions for advisory services, crowdfunding, peer-to-peer payments, and social investing are acknowledged but not considered mature. Some banks have more interest in these topics and have collaborated with technology companies to explore possible new business models. For example, Citigroup, Royal Bank of Canada, and Australia’s ANZ Bank have all announced plans to work with IBM’s Watson, the robot that made its name by beating humans on the television quiz show Jeopardy, to enhance customer advisory experiences.

“We always overestimate the change that will occur in the next two years and underestimate the change that will occur in the next 10. Don’t let yourself be lulled into inaction.”

— Bill Gates

Video advisory service is among the most controversial topics: While the United States and Nordic and Benelux countries strongly believe in this technology and customers are welcoming it, other regions such as Spain, Italy, France, and Germany are offering it to a less enthusiastic audience.

In general, enhancements to the product and service portfolio are just beginning. The next level will certainly encompass more complex services based on insights from various sources, such as social networks, mobile devices, apps, and harmonized internal data. Leading examples can be seen in innovative financial technology players around the world. For example, Vodafone and Safaricom created M-PESA to serve the largely unbanked Kenyan population. Users pay cash into their account at an agent, such as a gas station or supermarket, and then use their mobile phone to pay retailers or other individuals. M-PESA serves as an alternative to bank accounts and credit cards, which is especially appealing to the rural population. In 2012, about a third of the Kenyan population used M-PESA. Another focus point will be more effectively leveraging crowd intelligence to support existing advisory offers. Today, advisory concepts still center around the branch staff, either physically or by video. The next level could go even further, using renowned industry experts and incorporating the opinion of several thousand customers. Similar to Amazon’s automated next-best-product decision support systems, banks will use the purchase decisions of peers to help customers make a decision. Consider social investing: There are already several financial technology companies offering social trading or investing...
services that allow customers to trade synchronously with top traders based on their track record and the number of followers. Although banks have not gone that route yet, they are positioned to take a leading role in the advisory-driven investment business. Depending on the success of the new players, banks will have to react in a timely fashion and adjust their offerings accordingly, but this is not expected to occur within the next few years.

Nearly all banks we surveyed recognize a need to improve their offering with new value-added services, and they are working hard to simplify their core product portfolios (see figure 3).

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**Figure 3**

**Most banks see a need for new value-added services**

"What will change in regard to products and services offered?"

- **More value-added services**: 95%
- **Simplification of core products**: 82%
- **Proliferation of individual conditions**: 9%
- **Introduction of new products**: 5%

Source: A.T. Kearney and Efma global retail banking study

More than 80 percent are revisiting their complex product portfolio and radically rationalizing the product suite, from more complex product groups within loans to simple categories such as deposits. One Dutch bank, for example, has reduced savings products from more than 20 to just three. And Singapore-based OCBC Bank has tailored an offering entirely to students. FRANK by OCBC offers a simple, three-product portfolio—customized credit and debit cards, savings accounts, and tuition loans.

**Banking 360°: achieving an omni-channel experience**

Besides enhanced products and services, another focus area is the omni-channel experience. The traditional branch-based model is being replaced by an integrated channel approach that allows customers to conduct banking seamlessly across various channels, such as initiating a transaction in a branch and finalizing it in a mobile app. “We are implementing virtual relationship managers that are supposed to interact across the entire customer journey at more than 250 predefined events,” one Spanish bank executive said. And branch concepts are being reshaped worldwide—shifting away from uniform branches to more self-service outlets in the suburbs and flagship showrooms over specialized advisory stores in metropolitan areas. For example, FRANK by OCBC has branches that look more like retail stores, offering customers a stylish, trendy environment to browse products and ask questions. As this trend continues, branch density is expected to decline but not drop sharply as most branches will be used in a new way.

Having multiple channels for sales and service has become more crucial as point-of-purchase decisions have shifted upstream. Banks need to offer advice and recommend products when
the customer is considering making a purchase—and today’s customers are making those decisions long before they visit a branch. This requires a rethinking of advisory concepts. Branches can’t compete with the digital channel for advice because digital services promise to be available anytime, anywhere. And with customers doing most of their research and banking between 9 p.m. and 11 p.m. on weekdays and Sundays, no channel is more suitable for advisory services than digital.

Additionally, customers like to understand their peers’ opinions before making a decision. They no longer rely on the single view of a branch advisor and will challenge that advice with input from blogs, social networks, and public feedback forums. This trend goes beyond banking: Eight out of 10 Internet users look for health information online, making it the third most popular online activity (behind email and using a search engine), according to a Pew Research Center report. Yesterday’s digital trust issue seems to have evaporated. In fact, the digital channel is now challenging the credibility of bricks-and-mortar businesses.

While some players are clinging to the myth of superior branch advice, others are embracing the digital trend with a combined advisory model. For general advisory needs, they proactively create transparency about customer satisfaction and recommendations via portals, professional research tools, social networks, and peer chat functions. For more individual advice, they use chat functions with online staff members beyond normal business hours or offer video advice with overseas experts in addition to the core offering at branches. This increases the interactions between a bank and its customers without forcing customers to visit a branch. However, finding the right balance between virtual and in-person advisory services will be essential. For example, some banks are reluctant to embrace chat functions because of missing information about the return on investment. However, leading players are incorporating new concepts to offer around-the-clock advice, including customized in-person advice and peer recommendations bolstered by wisdom-of-crowd principles (see figure 4).

Figure 4
Banks are embracing digital ways to offer advice

<table>
<thead>
<tr>
<th>Time</th>
<th>Frequency of Use</th>
</tr>
</thead>
<tbody>
<tr>
<td>9 a.m.</td>
<td>Personal advisor call</td>
</tr>
<tr>
<td></td>
<td>Social network and peer-to-peer advice</td>
</tr>
<tr>
<td></td>
<td>Automated product recommendations</td>
</tr>
<tr>
<td></td>
<td>Comparison portals and online aggregators</td>
</tr>
<tr>
<td></td>
<td>Access to professional research tools</td>
</tr>
<tr>
<td>5 p.m.</td>
<td>Video advisory</td>
</tr>
<tr>
<td>8 p.m.</td>
<td>Chat and instant messaging</td>
</tr>
</tbody>
</table>

Once or twice a year
Daily or weekly

Source: A.T. Kearney analysis
Omni-channel integration poses a significant challenge for banks, in large part because of their legacy environment with siloed processes and IT systems. Thus, some banks are choosing a greenfield approach and setting up new digital banking entities with quick processes, integrated systems, and agile organizations. Examples from traditional banks include Axa Bank’s Soon mobile app, BNP Paribas’ digital Hello bank!, and Bancorp’s alliance with the all-electronic bank Simple. New companies are also entering the field, including MovenBank from the United States, Knab in the Netherlands, Alior Bank in Poland, and Fidor Bank from Germany. These digital banks promise a new customer experience with quicker processing, greater convenience, and anytime, anywhere availability, and they embrace social networks, mobile banking, and customer insights to better meet customers’ needs (see figure 5). Moving forward will mean choosing the best route: using existing structures and experienced organizations to further develop the digital proposition or taking a greenfield approach with lean processes and organizations. Both ways are possible but with different risks and opportunities.

Figure 5
MovenBank’s business model challenges every element of traditional retail banking

Virtual products and services
- No ATMs, debit cards, or credit cards
- Self-explanatory deposit and loan products
- Cash withdrawal and deposits possible from NFC-enabled retailers

Customer experience
- Banking reframed as fun by leveraging elements of computer games
- User experience is relevant and engaging to target digital-savvy consumers

Online and mobile channels
- No traditional banking channels (such as branches and ATMs)
- Mobile app and online account servicing (NFC technology leveraged to use mobile as payment device)

Social media
- Sign in with Facebook or Twitter
- Consumers’ social behavior evaluated to assess pricing and risk decisions
- Consumers rewarded for recommending MovenBank

Customer insight
- Questionnaire for behavioral profile, dynamically updated through consumer behaviors (spending patterns and balances)
- Behavioral profile used to help consumers achieve financial goals (such as savings) and price risk for credit products

Note: NFC is near-field communication.
Sources: MovenBank; A.T. Kearney analysis

Get Ready for the Long-Distance Journey

Disruptive changes have not yet occurred on the digital journey. Product and service portfolios have been enhanced, processes and procedures have been automated or supported by workflows, information and data have been shared across multiple channels, and branches have been redesigned and thinned out. And although this was costly, achieving the promise of a new banking experience through digitization will require even more change.
Big things ahead

The digital banking journey has just begun. So far, the playground has been limited to small initiatives, such as app suites, video advisory, and PFM tools (see figure 6). Big game changers such as a remodeled organization and work culture have not yet been addressed, but it’s just a matter of time—and it will fundamentally change the industry. It will mean breaking with tradition with customers no longer belonging to branches, IT driving the business, and new structures for revenue and pricing. As disruptive as it may sound, these shifts will bring opportunities to get something valuable in return: delighted customers.

Figure 6

The digital banking playground so far has been small

And with delight comes rapid change in a market that has so far been less than agile. Because the new banking experience will be much more enjoyable, next-generation customers will rethink their existing choices and jump on the bandwagon, the same way cell-phone users jumped from Nokia to Apple’s iPhone and Google-powered Samsung devices. Being among the first movers will be vital to maintain market position.

Beyond omni-channel: Vertical integration of processes and platforms

When it comes to digital banking, discussions quickly center around integrated multichannel or omni-channel offerings that make the customer experience seamless. Many initiatives and projects are attempting to tackle this challenge, but banks have a long way to go to achieve robust straight-through processing (STP). So far, work-around solutions allow existing clients to digitally open a new deposit account or get a “one-click loan.” For example, HANA Financial Group in Korea has a mortgage product that can be fully processed online in five steps from application to closing, not only reducing complexity on the bank’s side but also enabling customers to get loans faster and easier. As advanced as it sounds, this represents a minority—probably less than 10 to 15 percent of banks worldwide.
Furthermore, this STP capability applies only to simple products within an existing client base. If the request is from a new customer or is for more complex products, a lengthy manual process kicks in. Legislative hurdles are also a challenge when it comes to new customers. But remote identity verification capabilities are being developed by the dynamic financial technology community, in particular within the active payments space.

To fully achieve vertical integration, organization and governance will also need to be tackled. This area has only been marginally adjusted since the introduction of digital banking. While all banks acknowledge the importance of multichannel integration with a seamless flow of information, they have not aligned their internal organizations and governance mechanisms accordingly. For example, responsibility for profit and loss still resides mostly within the branch (see figure 7). “Our branches have great power and autonomy over customers, and the internal chargeback mechanisms to the branch profit and loss for online transactions do not really incentivize a digital operating model,” one Canadian bank executive said. In addition, the internal steering and cost-allocation mechanisms are often outdated and do not allow customers to smoothly shift around channels.

**Figure 7**

**Bank branches are still primarily responsible for profit and loss**

![Bar chart showing branch responsibility for profit and loss](image)

- **62%**: Branch has responsibility for profit and loss
- **31%**: Branch has partial responsibility for profit and loss
- **8%**: Branch has no responsibility for profit and loss

Note: Figures do not resolve due to rounding.
Source: Efma

Besides governance and steering adjustments, traditional approaches to channels, products, and customer segments will need to be reorganized and existing silos dismantled. For example, IT is still not part of the business, generally being asked to execute—not to develop—customer solutions. Silos also exist in product management, where dedicated teams develop solutions or define pricing structures that align with product group targets but may be misaligned from a customer or IT perspective. An all-inclusive review of existing structures will be required to support the new digital banking journey.

**Beyond lean: Back-end capabilities become strategic**

While many efforts are focused on the customer, digitization’s severe impact on the back end often gets overlooked. Integrated customer management, joint decisions, and STP processing will ultimately require a more central model, which will mean new challenges for the people
and skills. For example, back-office capabilities will be pivotal because information will reside centrally, interactions will be more centrally governed, and product recommendations will be generated by machines or central knowledge. To keep pace, back-office staff will need to develop highly efficient skills while at the same time be able to understand customers and shape solutions accordingly.

Legacy IT is another concern. Banks all over the world have already put massive amounts of money into consolidating back-end systems (and many are still in the midst of it) and integrating front ends, but the next wave of adjustments is just around the corner. The push to use big data to improve customer relationship management (CRM) capabilities is putting pressure on data quality and governance and dramatically increasing system performance, and yet only about one in four banks have immediate plans for big-data projects (see figure 8). The latest technologies, including in-memory processing, promise to transform huge, inflexible IT landscapes into faster, more agile environments where data analytics can be pivotal to success.

**Figure 8**

**Only about a quarter of banks have immediate plans for big-data projects**

<table>
<thead>
<tr>
<th>Planned big-data projects</th>
<th>Enterprise content management</th>
<th>Sentiment analysis</th>
<th>Cross-channel customer event management</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current</td>
<td>11%</td>
<td>10%</td>
<td>12%</td>
</tr>
<tr>
<td>Planned within one year</td>
<td>19%</td>
<td>17%</td>
<td>25%</td>
</tr>
<tr>
<td>Planned within one to three years</td>
<td>21%</td>
<td>10%</td>
<td>28%</td>
</tr>
<tr>
<td>No plans</td>
<td>28%</td>
<td>36%</td>
<td>13%</td>
</tr>
<tr>
<td>Don’t know</td>
<td>21%</td>
<td>27%</td>
<td>22%</td>
</tr>
</tbody>
</table>

Source: Efma

**Beyond banking: Value-chain disaggregation and new revenue models**

With digitization, another wave of value-chain disaggregation is likely to occur. The demand for more sophisticated elements within the value chain, such as managing customer insights and closing the capability gap banks have with industry leaders, will open up doors for new entrants. Big IT providers and niche financial technology players are entering the market with innovative solutions. And once customers get used to that kind of service, banks will need to react, either by shaping up their internal capabilities—a lengthy and expensive process—or by teaming up with new service providers.

In one possible scenario, the value-chain disaggregation could start with know-your-customer (KYC) services, where more advanced players provide deep customer insights from banking
transactions and a variety of other sources such as social networks, digital footprints, and shopping preferences to better understand customer needs and align CRM actions accordingly. After CRM, the next logical step could include risk-scoring activities, where the CRM provider delivers insights to better understand risks associated with customers. This scenario could ultimately split up core banking businesses, such as product development to external providers that know about customer preferences and associated risks, reducing banks to pure transaction handling—a highly regulated aspect that is less attractive to non-banks. Although this scenario may seem distant and improbable, it highlights the importance of building the right capabilities early enough to navigate toward the most desired outcome instead of waiting for others to make the first move.

Banks in Northern Europe and the United States are scrutinizing processes and entire value chains to determine which players will be in charge of the customer and which will be purely product providers.

Around the world, banks and non-banks are looking to work out new solutions and propositions to better serve their customers. The much talked-about move into banking by telco players and large players such as Google and Amazon is another scenario that could disrupt the industry. While legislation and regulation are still preventing fast-moving companies from fully entering the market, closer collaborations are likely to occur. For example, Google could provide deep customer knowledge and manage demands while the bank moves to the background as product provider and processing unit.

Disruptive changes are also expected in the product and service portfolio and in the revenue model. While banks are working on rationalizing their core product portfolio in terms of variants and specific offerings, the number of value-added services will surge as technology paves the way to support customers’ quest for convenience, individualization, and transparency (see figure 9).

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**Figure 9**

**Core banking products will become simpler, but value-added services will grow**

![Diagram showing core banking products and value-added services](image)

- **Core products**
  - Value-added services within credit cards
  - Postal services for high net-worth individuals
  - Personal loans
  - Point-of-sale finance
  - Commercial loans
  - Cards
- **Services**
  - Tax and retirement planning
  - Mobile apps
  - Segment-specific accounts
  - Savings and temporary deposits
  - Special purpose deposits
  - Mandated investments
- **Services with rich content tailored to individuals, automated or self-service**
  - Integrated app suite and personal finance management tools
  - Wallet solutions
  - Wisdom-of-crowd advisory
  - Person-to-person lending
  - Social-based services
  - Simple, modular products (one to two variants per customer need)

Source: A.T. Kearney analysis
This trend will radically disrupt existing business models. Banks will be able to offer a broader, richer, more efficient spectrum of services that are automated, self-directed, or even managed by third parties. And it will open up new revenue sources. The pricing for enhanced services could be mixed, with some services paid by the customers and others paid by service providers that want access to the bank’s clients, which could generate advertising income (see sidebar: Australia Bank Uses Spending Tool to Generate New Revenue).

Revenue and pricing models will also get an overhaul. For much too long, banks have relied on customers’ lack of understanding about their offerings, with complex solutions typically having the highest margins. However, digital banking will create transparency and comparability in price and performance. Pricing will be adjusted accordingly, and unjustified fees could fall by the wayside.

**Beyond machines: The cultural challenge**

One of the biggest challenges will be culture and people. Transforming from the traditional bankers’ club into a customer-focused, innovative, and fast player is seen as a major issue. “There is no Steve Jobs out there who can say, ‘Follow me,’” one Italian bank executive said. “At a traditional bank, you need solid business cases and 120 percent support from all stakeholders.” Addressing the attitude toward innovation and new ideas may be the best place to start. “Our inherent banking culture is preventing us from being truly innovative,” an executive at one Austrian bank said. “So we created a think tank outside the bank to design and decide new offerings, by bankers and non-bankers.”

Trial-and-error approaches are typically not suited to the conservative way of banking, but it may be required in a fast, digital world where first-mover advantages are worth more than a perfect business case. “Two main changes are required,” according to one German bank executive. “We need to incorporate a trial-and-error approach to banking and accept that in some cases the machine is the better seller.”

Getting staff to embrace digital as a way to improve efficiency and effectiveness is another issue. So far, they have not been given much incentive. In fact, some see it as a threat to their jobs and have begun boycotts. “The problem is that branch staff still considers digital as a threat that will ultimately take away their job rather than embracing new opportunities to better serve their customers,” one Spanish bank executive said. Two moves can pave the way: Install new decision-making authorities that allow for faster innovation, and get more buy-in from staff.

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**Australia Bank Uses Spending Tool to Generate New Revenue**

UBank, a division of National Australia Bank, has launched an interactive website with a personal finance management tool for customers and new value propositions for the bank. PeopleLikeU allows users to compare their spending habits with peer groups and national averages. Each spending category can be detailed so users can see how much is being spent and on what, such as food, travel, shopping, household expenses, and entertainment. This not only gives customers insight into their spending habits, but also gives the bank an opportunity to generate new revenue by allowing third parties to recommend their products in advertising space on the site.
Regional Differences

Banks worldwide are on the move. They may not be moving at the same pace, but digital banking is on every player’s agenda from the United States to Europe and Asia Pacific. However, regional environments are defining each county’s readiness for digital banking.

Our study sheds light on the regional differences in how ready the markets are and the approaches banks are taking. To learn more, we compared the digital readiness of 27 countries worldwide by taking a deep look at banking capabilities, market dynamics, customer readiness, and regulatory factors (see sidebar: About the Study).

We used insights from our interviews with leading bank executives and market research to pinpoint the hot spots for digital banking. The most developed environments are in the United Kingdom, Singapore, Denmark, Sweden, the Netherlands, the United States, and Australia (see figure 10 on page 14). These regions offer forward-thinking, nurturing environments for digital banking—be it the strong voice of customers, an advanced banking landscape, or tech-savvy financial technology markets.

The Netherlands, Australia, and Singapore show strong banking capabilities, including advanced digital offerings, strong financial positions, and digital structures while the United Kingdom strongly benefits from a very dynamic market with an attractive financial sector and aggressive technology-oriented companies spurring change in banking solutions.

From a customer perspective, the markets in Singapore, Sweden, and Denmark are the most advanced with many digital natives, high smartphone penetration, and strong e-commerce shopping behavior (see figure 11 on page 15).

Within Europe, there is an interesting mix of readiness. In some regions, banks are pushing digital topics, but other factors are not following at the same pace. Consider Spain, for example, where digital banking offerings are already advanced but customers and the regulatory environment are lagging behind.

About the Study

This report analyzes the impact of digital banking worldwide. About 50 in-depth interviews with leading retail banks all over the world were conducted to better understand their approaches and motivation toward digitization (see figure). Interviews focused on the impact on products and services, organization, culture, operations, and IT.

The report also includes Efma and A.T. Kearney research on digital readiness along with examples and best practices from digital banking all over the world.
In Eastern Europe, especially in Poland and the Czech Republic, some banks are actively pushing digital banking and are making good progress. Customers are embracing the trend and using new options such as mobile banking and crowdfunding. But overall, it’s happening on a small scale. In Russia, banks are less euphoric about digital banking and focus more on consolidating and rationalizing existing platforms.

The environment in Western Europe, including Germany, France, Switzerland, and Austria, is slightly less ready. Banks are looking into digital options but have not yet made step changes,
with bolder moves such as BNP Paribas’ Hello bank! or Axa’s Soon being the exceptions. Here, the branch network is still seen as important because of an older population that has more traditional beliefs.

North America is rife with digital exploration and innovation, particularly in the areas of mobile banking and payments. However, in both Canada and the United States, legacy technology environments and siloed organizational structures stifle banks’ ability to transfer digital innovations from the laboratory to the marketplace. While many banks continue to grapple with what to do about expensive and outdated branch networks, leaders such as USAA continue to focus on integrating digital innovation into their business culture and standard operating procedures.

Southern Europe and the Middle East are also actively exploring digitization, in particular investing strongly into improving CRM capabilities and value-added services. Nevertheless, the
environment is less ready, given the constraints of the financial crisis and a population that lacks trust. In summary, we see a north-south decline of digital banking readiness in Europe down to the Middle East.

However, being ready means more than just having the appetite for digital banking. It comprises the entire banking environment, technology developments, competitive challenges, customer demands, and regulations. Our Digital Banking Readiness Index (DiBRix) assesses the readiness in 27 countries by analyzing four dimensions: banking capabilities, market dynamics, customer behaviors, and the regulatory environment. More than 30 factors were used to calculate one readiness figure that can be used to anticipate a region’s digital banking readiness.

While all four dimensions influence a country’s overall readiness, there are some sensitive variables in the mix. For example, if the banking market is highly concentrated—with the market share of the five largest banks (CR5) greater than 70 percent—and one of the leading banks makes a significant move toward digital banking, the rest must rapidly follow or risk losing momentum. The same applies for customer readiness. For example, countries with a young population and high affinity for mobile or social networks can quickly turn a market upside down. Consider the United Arab Emirates. The region has a young demographic with a median age of 30 years, smartphone penetration of more than 60 percent, great Internet access, a strongly growing e-commerce segment, and socially networked consumers. While banks are testing new digital solutions and continuously improving digitization in their core operations, the market dynamics are still low. Regions like this may quickly turn toward a far more digitally banked world once the market has experienced some breakthrough innovations.

In the Netherlands, **big banks are the primary players** pushing digital banking.

In Australia, the picture is different. Banks are well prepared with high penetration in online and mobile banking and fresh, innovative solutions, solid financials, and digital-oriented structures, but their customers and market dynamics are less ready. However, this scenario could quickly change as Asia Pacific customers tend to adapt rapidly to new trends and market dynamics can quickly heat up.

In the Netherlands, big banks are the primary players pushing digital banking. Take, for instance, the collaborative approach of the country’s leading banks to jointly push the development of near-field communication mobile payments. New solutions such as Rabobank’s MyOrder is enabling small and medium-size enterprises to participate in the m-payment space without major investments in infrastructure.

Within the individual categories, readiness may look quite different. Consider Switzerland. Customers seem to be more ready for digital banking than most of their banks are, as seen by comparing customer behaviors with banking capabilities. For example, banks still rely on non-digital structures (based on branch usage and operational efficiency indicators) while many of their customers are equipped with the right devices and the right mindset. (Smartphone penetration is above 30 percent, and more than 75 percent use social networks.) The attractive Swiss financial sector with its high concentration among the leading banks (75 percent CR5) could quickly evolve into a target for more digital-savvy players. Or one of the leading banks could make a significant move into digital, forcing the remaining players to quickly follow.
Outlook and Action Plan

Advancing in digital banking is not just a question of how, but also when. In the past, overly aggressive moves have more or less resulted in sunk costs. Avoiding this will require understanding and anticipating market movements.

Seizing the improvement areas

Two moves can propel players toward digital banking excellence: Improve customer satisfaction on the outside with enhanced products and services, fast and effective interaction and processing, and excellent price-performance ratios. And work on the inside by aligning internal structures, cleaning up IT and processes, and finding appropriate revenue models.

For the outside improvements, benchmarking against best practices can shed some light on your market position while at the same time identifying potential collaboration partners along the value chain. These best practices can come from competitive banks or from new innovative players.

For inside improvements, optimizing structures, processes, and IT will take multiple initiatives—from product ratification, process and IT harmonization, and organizational alignment to new governance mechanisms and a new work culture. Defining the targets is usually a good place to start. Where are you positioned in terms of processing speed, STP ratios, decision-making processes, organizational efficiency, product pricing, and profitability? Comparing with market best practices is also recommended here, looking beyond traditional banks. What would leading best-practice companies demand? How are direct banks prepared? (See sidebar: Direct Banks Could Be the Winner After All.)

All these insights can be used to define the targets and road map for digital banking improvements.

Direct Banks Could Be the Winner After All

It’s been quiet around direct banks lately. The financial crisis and the subsequent phases of ultra-low interest rates have put pressure on existing business models. With more and more banks turning away from bricks-and-mortar business and new digital players trying to tap into the banking and payment markets, the competitive advantage seems to be melting away.

However, despite these issues, direct banks could turn out to be the winner in this dynamic market. Traditional banks have a long way to go to revamp their organization, culture, and operational and IT capabilities to meet the requirements of the new digital banking experience—and yet direct banks are already built on fast and efficient structures.

The focus for the direct banks that lead the way will be on enhancing their offering to create a better customer experience with new services such as personal finance management tools, point-of-sale wallet solutions, and digital advisory concepts with peer-to-peer or crowd-intelligence principles. This will require much less effort than transforming an entire organization, including branch governance and culture, leaving traditional banks at a disadvantage.

The direct-bank threat is more serious than the threat from non-banks, such as Google entering the market with its Google Wallet app, and the strict regulations that come with banking are still an obstacle for retail companies to fully enter the banking market.
Finding the right timing

To get ahead on the digital journey, timing is everything. Banks that have rushed into hype themes in the past have experienced push-back from customers who were not quite ready or from the overall market, which was not yet as supportive as required to transform the hype into a clear trend. A deep understanding and anticipation of the digital environment is necessary to launch the right moves at the right time.

The DiBRix can be used to understand the overall environment and to prioritize actions, depending on the overall readiness but even on a more granular level within the four dimensions. The right moves could be completely different for players in an advanced environment with high digital readiness as opposed to those in countries where customers are not ready and legislation doesn’t favor pushing further into digital.

Three scenarios explain how the index can be used to choose the best road map (see figure 12).

Figure 12
Scenarios for digital banking readiness

Sprint

These banks are not prepared to switch to a more digitally oriented banking model, but the market competition (non-banks and financial technology providers) and customers are ready. Regulations are indecisive, which works in favor of the banks, but this situation is not to be underestimated. Add some accelerators into the mix, such as a young population with high mobile affinity or high market concentration among banks, and it could be explosive.

Action plan:

- Focus on customer impact initiatives, including product enhancements, value-added services, and fast processing.
- Collaborate with non-banks to pick up the pace.
- Remove internal barriers in the organization, decision processes, and culture.

Many players face such a situation in the United Kingdom, the United States, Poland, Switzerland, Austria, and Canada.
**Siesta**

These banks are pushing strongly into digitization. Solutions and service models have been developed and introduced, but the market and customers are not there yet. The supporting environment is missing. Perhaps the point-of-sale technologies are not mature enough, customer income levels are too low, or political stability is not a given. All this may indicate that the best course of action is to slow down and take a rest.

**Action plan:**

- Focus on internal excellence: hone STP, define moments of truth for customer delight, and align organizations and governance.
- Potentially incubate market dynamic: consider funding the financial technology startups into the market.

This situation can be seen in some players in the Italian, South African, and United Arab Emirates markets.

**Marathon**

These players are less advanced in digital banking readiness, perhaps because of strong legacy structures or financial instability, but they are also bogged down in a slow-moving environment, such as where customers prefer the classic branch approach or the market is not hot for digital.

**Action plan:**

- Pursue a consistent and gradual digital transformation.
- Focus on cleaning up legacy systems. Work on inside areas, including organizations, IT, processes, and culture.

Examples in this category can be found in Germany, France, and Spain.

**The Road Ahead**

Banks will become more digital. It’s only as a matter of time. As customers, competitors, and even regulatory agencies push in this direction, the promise of anytime, anywhere banking with transparency and convenience will ultimately bring together today’s branch-based traditional players with the no-frills offers of direct banks and innovative financial technology players, all coming from different directions. And it’s hard to say who will arrive first.

For traditional banks carrying a heavy heritage, it will be crucial to overcome internal obstacles to achieve fast, robust decision making and processing, customer-centric channel management with revised governance mechanisms, and agile, high-performance IT landscapes. But the cultural barriers may be even more challenging: a new mindset is required in many regards. Better and faster innovation, fair and transparent product and service offerings, and new sources of revenue need to be tapped into.

For direct banks, the challenge will be refreshing their image from a low-cost provider relying primarily on self-service to a valuable player with rich products and services that bring customer satisfaction and convenience. In some cases, rebranding may be required, similar to ING Direct’s rebranding as Capital One 360°.
With all the non-banks and other financial technology players also being part of the mix, we will definitely see more collaboration scenarios between banks and innovators. These partnerships will accelerate the digital journey as their offerings show customers fascinating new ways to improve their banking experience. Banking will encompass a wider range of services with multiple parties involved while at the same delivering a seamless customer experience. This will ultimately create banking that is convenient, fast, and proactively meeting needs—a stark contrast to today’s more reactive and less-transparent business model.

Forward-thinking players will carefully consider when and how to move forward, with an eye on the regional banking landscape and an understanding of their most unrelenting internal roadblocks. Will organizational agility be the most daunting obstacle to digital banking, or will it be the lack of centricity in crucial customer-facing activities? What about IT capabilities?

Putting all this into the overall context of the competitive market and customer expectations will define the way forward as the digital journey continues.

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