Customers in the spotlight

How FinTech is reshaping banking

Global FinTech Survey 2016

76%

More than three in four banking respondents fear some part of their business is at risk to FinTech

42%

Many banks engage in joint partnerships with FinTech companies

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Key messages

Contents

Consumer banking is the sector most likely to be disrupted by FinTechs in the financial world

Banks see changing customer needs as the top impact FinTechs have on their business

The majority of banks (71%) predict more than 60% of their clients will use mobile applications within five years

Loss of market share and margin pressure are the key threats in the banking industry

A vast majority of banking respondents (76%) fear some part of their business may be lost to FinTechs

Banks are the most active (42%) of all financial sectors in engaging in joint partnerships with FinTechs and in setting up venture funds to fund FinTech companies

Introduction

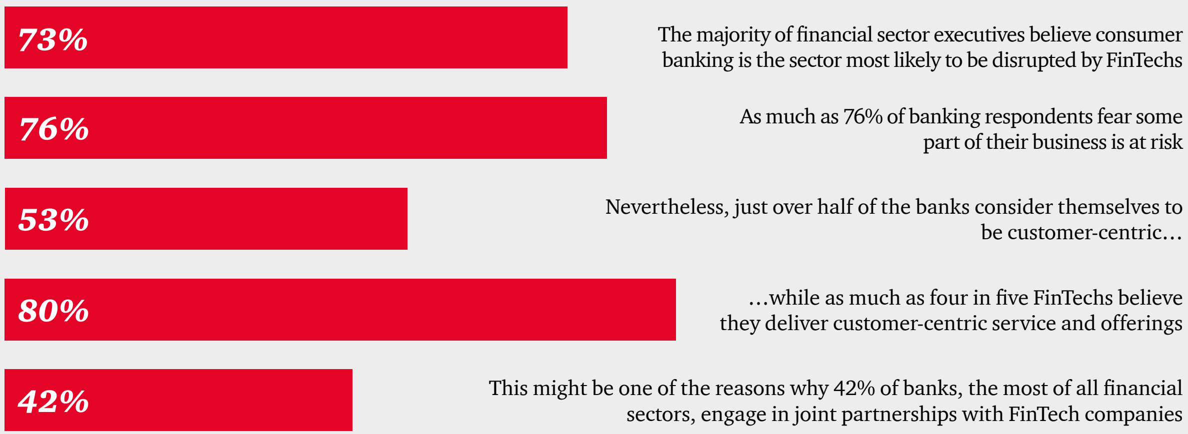
Consumer banking is on the verge of disruption, much of which is led by the disaggregation of simple products and service offerings.

Everyone agrees that there is a clear need for greater focus on the customer, but start-ups do it better. While new entrants have identified the need for increased customer-orientation as an opportunity and are building solutions to address this in the market, traditional banks are still lagging and delivering incremental improvements. New entrants, on the other hand, do not just focus on customer service in the traditional sense, but understand and meet evolving customer needs with dynamically different product design and delivery.

Customers are redefining their expectations, taking their cues from other industries that offer multichannel access, product simplicity, seamless integration and 'segment-of-one' targeting. They want convenience, personalisation, accessibility and ease of use. They want to feel like their bank is anticipating their needs, not bombarding them with product offerings. They want transparency and no surprises in terms of fees.

FinTech start-ups go directly to the end-user, bypassing banks altogether. 75% of survey respondents see an increased focus on the customer as the most important area of impact. By observing

Figure 1: Highlights from the PwC Global FinTech Report 2016



Source: PwC Global FinTech Survey 2016

and often experiencing first-hand what banks offer – or do not offer – new entrants pick off segments of the banking sector and develop narrowly defined, but highly effective solutions to manage customer expectations. Competition between banks and new entrants may give way to direct cooperation across the FinTech ecosystem. Opportunities exist for partnership and cooperation that would leverage each other's strengths, whether in product design and development by the start-ups, or distribution and infrastructure capabilities by banks. However, several major impediments inhibiting business relations between banks and FinTechs remain. We see both sides coming to the realisation of a new, mutually beneficial relationship that is possible, but it is still in the early stages of execution.

1

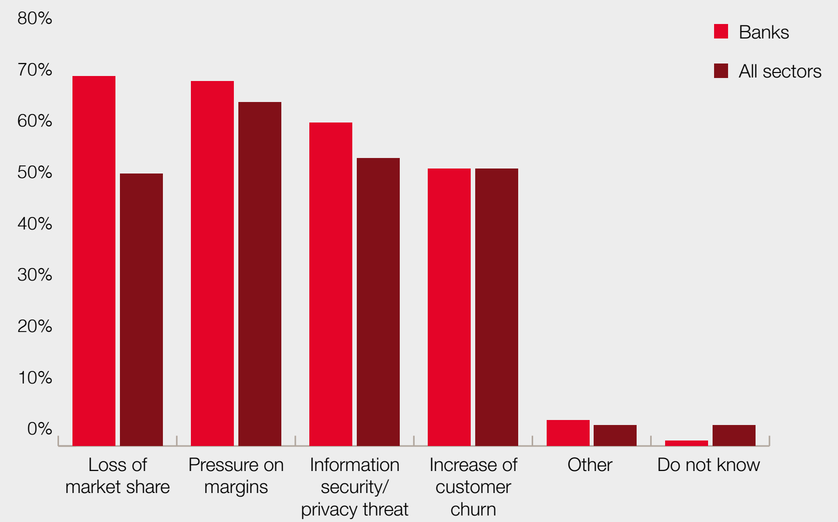
Consumer banking braces for disruption

Consumer banking, once viewed as the bastion of stability in financial services, is now being identified as the most likely financial sector to be disrupted by FinTech over the next five years.

The very simplicity that underlies banking products and processes for saving, lending, and business services renders the sector ripe for disruption. The majority of financial sector executives (73%) perceive consumer banking as the one most likely to be disrupted by FinTech.

New entrants see opportunity in disaggregating the components of traditional banking and offering targeted solutions with better servicing to both retail consumers and businesses. In parallel, the threats posed by FinTechs have the ability to disrupt four categories of incumbents' business – market share, margins, information security/privacy and customer churn – at higher rates when compared to other financial sectors (figure 2).

Figure 2: What are the threats related to the rise of FinTech within your industry?



Source: PwC Global FinTech Survey 2016

2

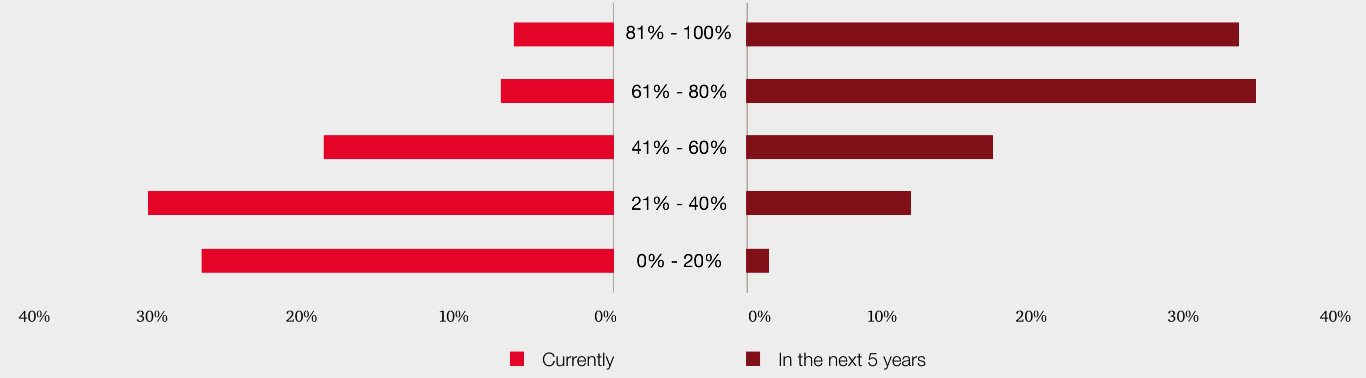
Reinvented customer service

Some people still prefer human interactions in certain parts of the process. However, a viable digital approach is now mandatory for banks wishing to compete across all consumer segments.[1]

Traditional players are still in the early stages of customer-oriented solutions, at least when compared to what FinTechs propose. Only half of the respondents from the banking sector (53%) believe they are consumer-centric, compared with over 80% for FinTech survey participants.

By prioritising 24/7 access, FinTechs offer services available via non-traditional channels, such as social media, that empower customers to a great extent. FinTechs also stand out from the traditional crowd with their focus on ubiquity and omni-channel offerings. New entrants understand the need to design product offerings not by siloing, but by considering and fulfilling the various needs of the customer at different points along their journey.

Figure 3: What is the percentage of your bank's clients using the app at least once a month?



Source: PwC Global FinTech Survey 2016, banking survey participants

Over 90% of banks expect growth in the usage of mobile applications, much higher than any other financial sector. 71% believe that over the next five years, more than 60% of their clients will be using mobile applications at least once a month to access financial services (figure 3).

"Banks will be judged against all customer experience, not just other financial services"

Director/Head of Department at one of the biggest banks in Australia.

[1] PwC, *Consumer lending: understanding today's empowered borrowers*, 2015.

3

Shower of smart solutions

A major concern for traditional players is FinTechs going directly to retail end-user and bypassing banks altogether. They offer attractive solutions to client sectors often neglected by traditional banks.

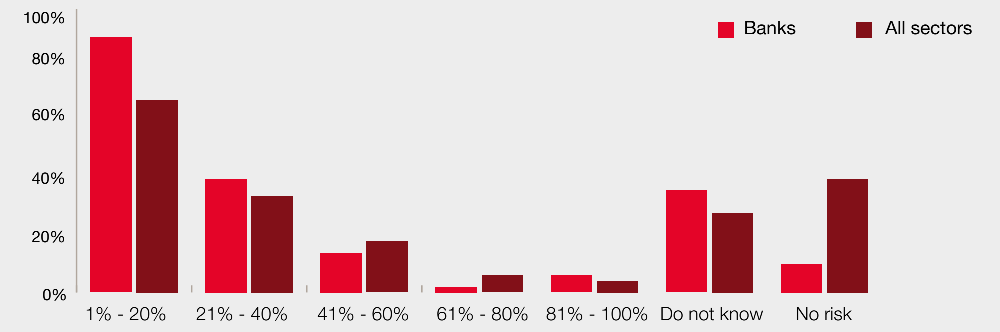
By observing and often experiencing first-hand what banks offer – or do not offer – new entrants are targeting segments that need to most urgently focus on the customer. By developing narrowly defined, but highly effective solutions, they have managed to step into and take over segments neglected by traditional banks in terms of offerings. In fact, almost 80% of executives believe that at least some portion of their business is at risk to FinTechs (figure 4). In particular, FinTechs are offering:

Solutions for customers with no or poor credit scores who are unable to get loans. The status quo has driven FinTechs to lending innovation based on alternative credit decisioning methods, the use of non-traditional data sources and powerful data analytics to price risks, rapid customer-centric lending processes, and lower operating costs.

Peer-to-peer (P2P) marketplaces for customers unable to secure loans from the traditional sources. P2P lending has experienced tremendous growth in the past five years, during a period in which most banks tightened their credit standards and their reputations were tarnished as a result of the financial crisis. Even though 2016 has not been very productive so far, the P2P market has declined due to a global economic and junk market slowdown and a massive case of fraud in China. Even though the growth rate has slowed down, we still project the peer-to-peer market to be worth $150 billion by 2025.[2]

Personal finance management tools. The inability of customers to manage or track expenses across banks led to a rise in the popularity of personal financial management (PFM) tools and aggregators.

Figure 4: What percentage of your business is at risk of being lost to standalone FinTech companies within 5 years?



Source: PwC Global FinTech Survey 2016

Banks will need to develop a better understanding of their customers' preferences in order to maximise their value potential. They need to do a better job of connecting the dots internally to obtain bank-wide views and actions based on their customer relationships. For example, by analysing a deposit in a customer's account, they can respond to a salary increase and send a letter of congratulations with an offer of a premium card with a higher credit limit.

[2] PwC, *Peer-to-peer lending*, 2015.

"The threat of FinTech is the impact it will have on customer expectations towards banking services"

Director/Head of Department at one of the leading banks in the Netherlands.

4

Reaching out to business clients

A noticeable shift towards enterprise FinTech is also underway. More players are focused on B2B solutions than ever before.

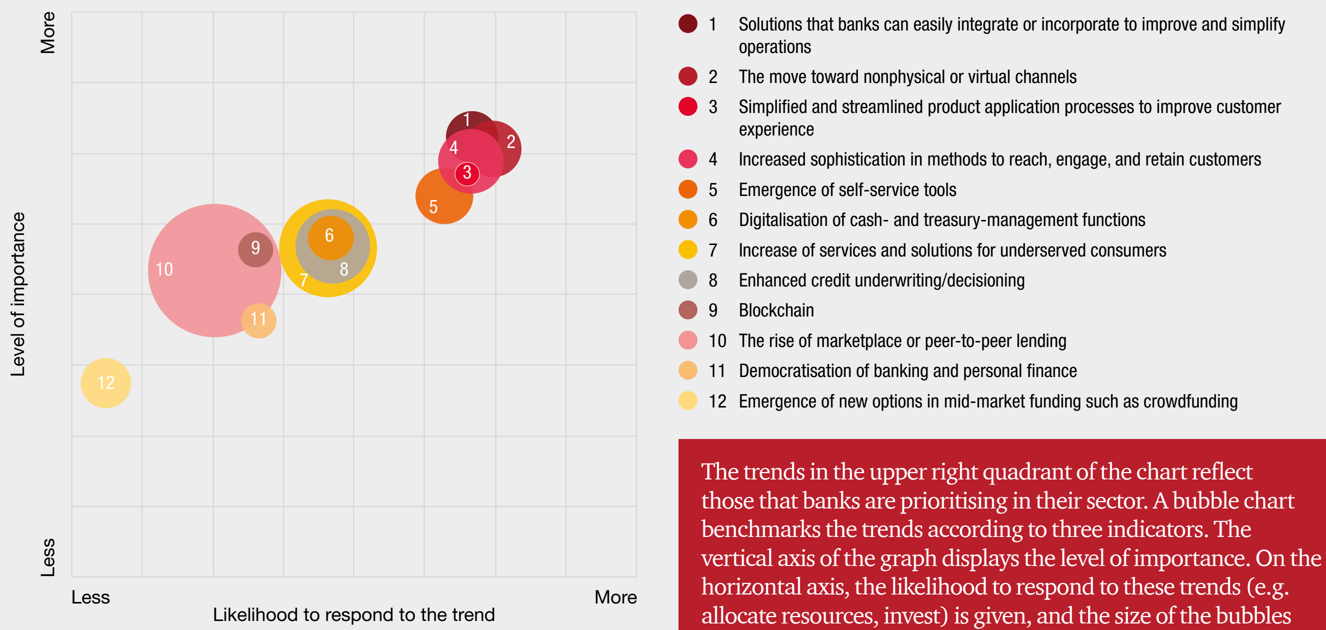
While plenty of start-ups continue to focus on engaging retail customers with innovative solutions, other FinTechs delve into lower profile or "unglamorous" back-office functions, such as invoice automation, lending and commercial solutions for SMEs or micro-businesses. B2B solutions get at the heart of what often ails legacy financial institutions: antiquated technology that is cumbersome to maneuver. Banks are increasingly utilising open development and Software-as-a-Service (SaaS) solutions offered by FinTech start-ups in an effort to easily integrate and streamline operational capabilities and move toward digital/mobile delivery. The incorporation of application program interfaces (APIs) enables third parties to develop value-added solutions and features to assimilate with bank platforms.

Easily integrated solutions that can improve and simplify operations are rated highest in terms of level of importance and the move towards non-physical or virtual channels is ranked highest in terms of likelihood to respond (figure 5).

Figure 5: Trends in the banking industry ranked by importance and likelihood to respond

How important are these trends for your industry and how likely are you to respond to them? (e.g. allocate resources, invest)

The size of the bubbles is proportional to the number of related FinTech companies as assessed by the DeNovo platform



Source: PwC Global FinTech Survey 2016 and DeNovo – see in Appendix the definitions of the above-mentioned trends.

The trends in the upper right quadrant of the chart reflect those that banks are prioritising in their sector. A bubble chart benchmarks the trends according to three indicators. The vertical axis of the graph displays the level of importance. On the horizontal axis, the likelihood to respond to these trends (e.g. allocate resources, invest) is given, and the size of the bubbles is proportional to the number of related FinTech companies associated with the trend.

5

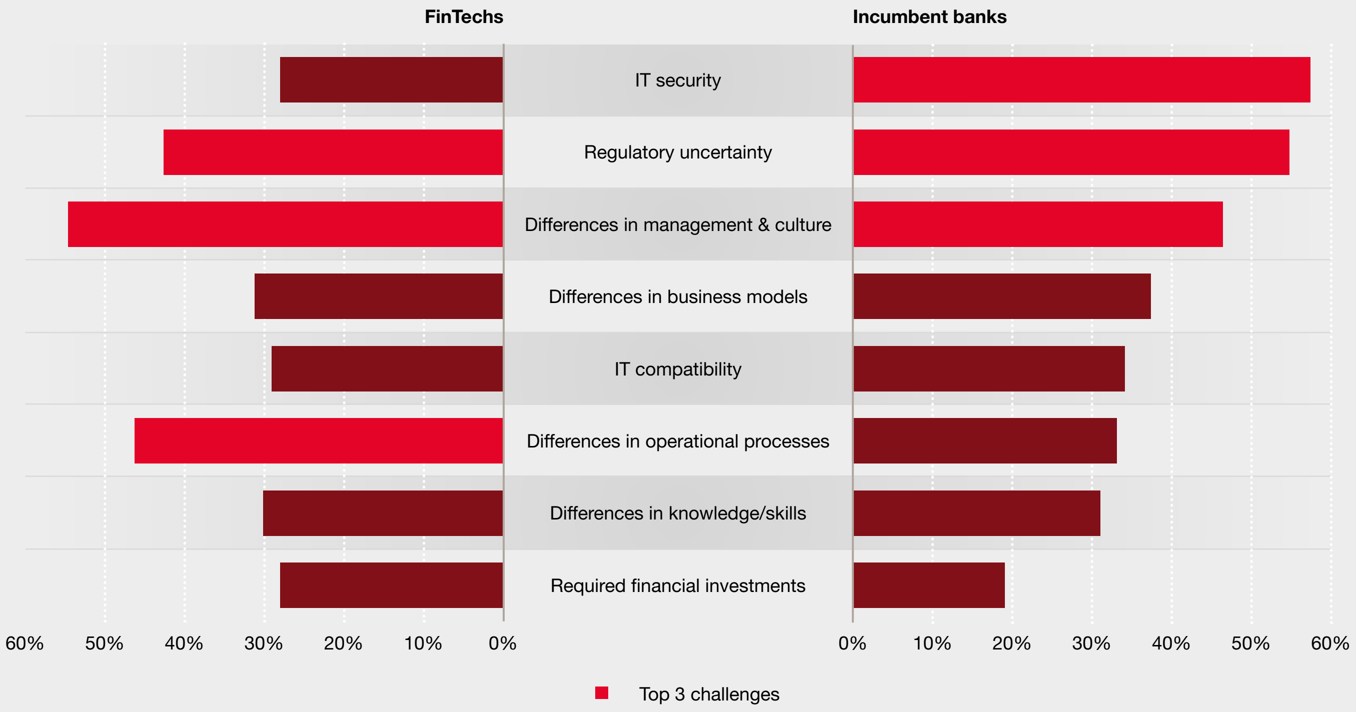
Paving the way for a win-win partnership

Competition between banks and new entrants may give way to direct collaboration across the FinTech ecosystem.

In this case, both parties should profit. Potential opportunities span from product design and development by the start-ups to distribution and infrastructure capabilities by banks. However, several major impediments inhibit business relations between banks and FinTechs. From the banks' perspective, FinTechs lack the proper IT security and regulatory certainty, while FinTechs believe banks can be hard to work with due to differences in management and culture as well as differences in operational processes (figure 6).

Misalignments aside, 42% of banks are already engaging in joint partnerships with FinTech companies, more than any other financial sector. Banks are also the most active of all industries in setting up venture funds to fund FinTech companies (19%), and are the financial industry's frontrunners (together with fund transfer & payments companies) in white-labelling FinTech services.

Figure 6: What challenges did/do you face in dealing with FinTech companies/incumbent banks?



Source: PwC Global FinTech Survey 2016

Conclusion: Customer experience is moving into the spotlight

Cooperation between traditional banks and new entrants is important, but agreeing on optimal ways of working can take time. Meanwhile, banks should focus on delivering a reinvented and improved customer experience.

Clients expect offerings, contacts and overall relationships with banks to be seamless, and address their particular needs. Even if there is no simple "one size fits all" solution, there are some universal steps that will help banks get closer to what their customers expect.

Banks should start simplifying products and services to facilitate comparisons between the market players and reduce client confusion. In parallel, it is crucial that banks design products with the user experience in mind instead of the common "processes as design guidelines" approach. Finally, banks should listen to customer feedback and use it to develop appropriate offerings in a timely manner. These actions must be taken regardless of the FinTech-caused disruption.

Traditional players may already have some streamlined and digital capabilities, but they should integrate their multiple digital channels into an omni-channel customer experience, while leveraging their existing customer relationships and scale. Banks need to provide holistic solutions by tailoring their offerings to customer expectations. They can support these efforts by using newfound digital channels to collect customer data to better predict customers' needs, offer compelling value propositions and generate new revenue streams.

Cooperation with FinTechs could definitely make the task of becoming customer-centric easier to achieve as the new entrants have important complementary skills. On their side, FinTechs could benefit greatly from partnerships with traditional banking players that possess insightful customer data. Spending patterns and wealth data could be important indicators for FinTechs tailoring the next game-changing solutions. Further, leveraging legacy banks' customer reach and regulatory prowess could allow FinTechs to focus on what they do best – meeting 21st century customer needs in new and creative ways.

Finding the "sweet spot" between competition and co-operation where traditional banks and FinTechs truly collaborate might be cumbersome, but once a *modus operandi* is established, both parties will profit. Only then will the banks be able to stem the tide of business model disaggregation by new entrants in the FinTech space; by partnering with well-established traditional banks, FinTechs will gain customer trust, client data and recognition that will allow them to thrive.

"The banks of the future will be software companies"

CEO of one of the leading banking groups in Latin America.

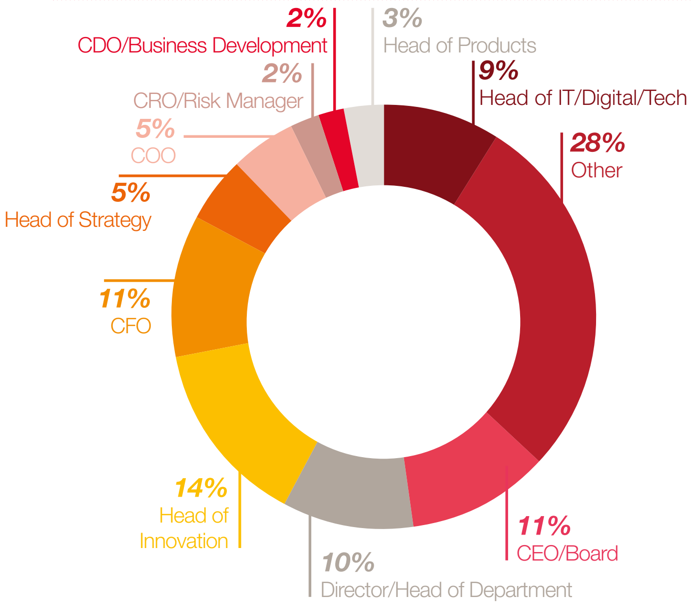
Appendix
Participant profiles

The 2016 PwC Global FinTech Survey gathered the views of 544 respondents from 46 countries, principally Chief Executive Officers (CEOs), Heads of Innovation, Chief Information Officers (CIOs) and top management involved in digital and technological transformation, distributed among five regions.

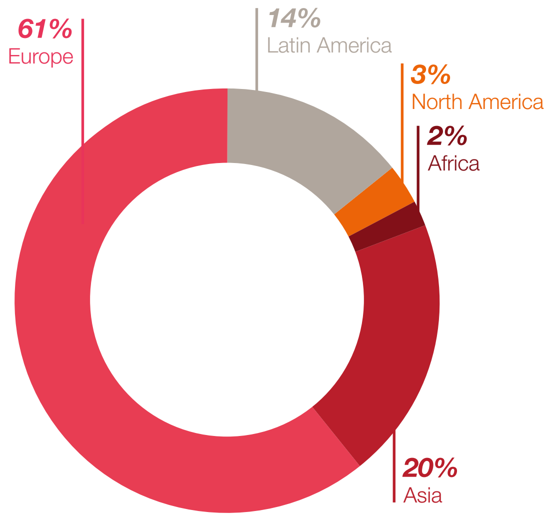
The banking-focused cut is based on the responses of 163 respondents from banks around the globe.

Breakdown of banking survey participants

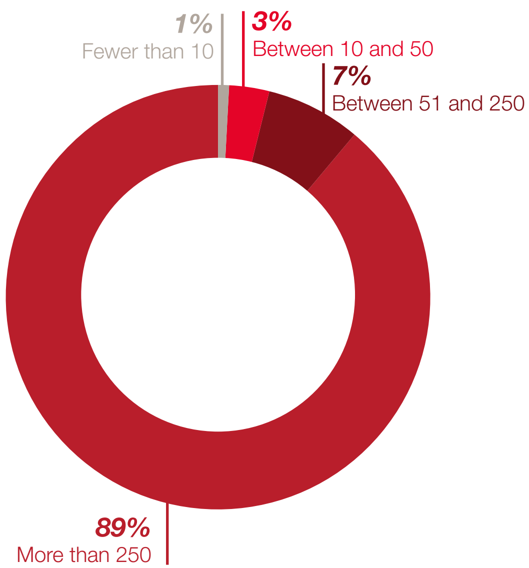
by type of respondent



by geographical location



by company headcount



Summary of the FinTech-related trends

What is DeNovo?

DeNovo represents the next generation of strategy consulting – a new platform powered by Strategy&, PwC's strategy consulting team that is focused on FinTech. The rapid emergence of disruptive technologies and new business models requires a modern way of delivering strategic advice when and where you need it. Whether you are in the board room or on a phone call with your CEO, DeNovo provides you with answers in real-time. Relevant content and insights are delivered to you via web, mobile and direct interaction with our team of innovation strategists.

http://www.strategyand.pwc.com/denovo

DeNovo's Team is tracking emerging trends in FinTech to explain which start-ups, technologies, trends, and new market entrants are relevant to the banking industry and more importantly, why. The trends highlighted below are a snapshot in time of the most relevant ones for the sector. For an updated view, please subscribe to the DeNovo platform.

1. The rise of peer-to-peer (P2P) lending	Increased levels of technology have enabled an increase in lending from one individual to another without an intermediary.
2. The increase of services and solutions for underserved consumers	Technology has lowered the cost of providing services to customers that are currently underbanked, such as those in rural Africa where many rely on informal banking services.
3. The enhancement of credit underwriting/ decision making	More granular data are enabling financial services providers to more accurately assess and price risks.
4. The implementation of solutions that banks will integrate or incorporate to improve and simplify operations	Banks are adopting new solutions to improve and simplify operations. For example, APIs enable third parties to develop value-added applications for company's platforms, artificial intelligence is enabling companies to extract greater customer insights, employees and intelligent machines are integrating to work as a team, banks are expediting the deployment of digital delivery.
5. The increased sophistication in methods to reach, engage, and retain customers	Rise of alternative distribution and marketing channels for awareness and lead generation. Engaging customers through gamification techniques in a collaborative environment leading to better customer experience and reflecting in retention.
6. The emergence of self-service tools	Increase of customer autonomy in performing every service without human interaction. Self-service tools, such as internet banking and apps, are becoming more popular.
7. The move toward nonphysical or virtual channels, including mobile channels	The internet and improvements in technology have enabled banks to increasingly provide traditional banking functions through virtual channels. Virtual banking utilises on-line and mobile platforms to integrate and simplify the customer banking experience. Virtual banking platforms equip customers with on-demand access to manage bank accounts, pay bills, apply for loans, open new accounts, and perform other banking activities through a single portal. Banks are using these channels to collect data from customers, generate new revenue streams, and offer compelling value propositions.
8. The digitalisation of cash- and treasury-management functions	Cash and treasury management includes the administration of external and internal funds, cash flow management, and corporate finance policies and procedures. The digitalisation of cash and treasury management functions utilises online platforms to disrupt the traditional cash and treasury models, creating new revenue streams and value propositions. Cross-border payment transfers for businesses, foreign exchanges, and invoice management are a few of the functions that are enabled primarily through the advent of online platforms. For example, organisations are developing new processes to perform international money transfers using mobile wallets and cryptocurrencies to get money to customers faster and cheaper.
9. The democratisation of banking and personal finance	The democratisation of banking and personal finance describes the shift in which customers are taking control over their financial health and are seeking new channels and solutions to assist in this process.
10. The simplification and move toward streamlined product application processes to improve customer experience	The consumer product application process (i.e., loan origination) has been streamlined with the emergence of cloud-based lending solutions and electronic bank account management systems which automates the loan origination process and increases overall transparency in the lending process. The move towards such solutions improves customer experience by reducing the amount of manual work, cutting down time and reducing errors.
11. The rise of crowdfunding/seed funding	New funding options have emerged in mid-market, such as P2P lending and market place lending platforms.
12. Blockchain	Use of distributed and decentralised ledger technology in which transactions are recorded in order to improve payments, clearing and settlement, audit or data management of assets. There is also the possibility to create a so-called "smart contract" using blockchain technology. This is essentially a contract that is translated into a computer program and, as such, has the ability to be self-executing and self-maintaining.

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