APU INSIGHTS
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GLOBAL TRENDS & CHALLENGES IN RETAIL BANKING

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Executive Summary

For banks globally, 2018 could be a pivotal year in accelerating the transformation into more strategically focused, technologically modern, and operationally agile institutions, so that they may remain dominant in a rapidly evolving ecosystem. This metamorphosis is far from easy as most banks grapple with multiple challenges: complex and diverging regulations, legacy systems, disruptive models and technologies, new competitors, and, last but not least, an often-restive customer base with ever higher expectations.

The banking sector is no stranger to digital transformation. With internet banking widely adopted by retail customers, mobile banking followed through as the dominant channel for personal banking. This change still maintains its momentum and is growing to this day. Open banking, public/private cloud, distributed ledgers and Artificial Intelligence (AI) technologies, all push the boundaries farther and faster than before. To this end, banks are trying several different strategies to address these changing technological and customer needs. Many choose to build new digital banks from the ground up whilst other have decided to work in partnership with FinTech specialist providers.

In this context we examine the challenges that most banks face today, taking into consideration the most important factors that may have significant impact on the long-term growth of banks. These factors are the following:

- Customer centricity,
- Regulatory recalibration,
- Technology management,
- Mitigating cyber risk,
- Fintechs and big techs, and
- Reimagining the workforce.

Key Findings

- The advent of FinTechs coupled with a growing digital adoption, ushered a wave of innovation into the retail banking that increased possibilities of connected offerings and superior customer experience.
- To promote innovation and competitiveness in the retail banking, regulators around the world are encouraging open banking.
- Previously, Application Programming Interface (APIs) were used primarily in private or partner-specific applications; but now, banks are using open APIs to connect with various third-party providers.
- The banking industry has always been under pressure for margins and regulatory requirements among others; however, last decade has witnessed the rise of a new set of challenges such as increased customer expectations, FinTechs and rapid digitization.
- Internet channels such as websites, mobile applications, and social media are heavily utilized by banking companies in order to interact with customers.
- Banks have been hampered by new forms of competition, regulation and increasing security concerns.
- Banks use data to drive competitive new sales and service channels and to improve customer experience which benefits both customer and bank.
- Global banking sector M&A volumes and values fell by 16% and 34% respectively in 2017, reflecting a continued move away from megadeals. However, signs of strength were evident in mid-market M&A, as well as the payments and FinTech segments.

Structure of the Report

This report is a comprehensive assessment of trends and challenges in retail banking sector.
The rest of this report is structured as follows:

Section 1

Industry overview focuses on the retail banking definition and the characteristics of retail banking. More precisely, it provides detailed information concerning the products and services of retail banking, the development and changes, and the pillars of retail banks. Moreover, it represents the performance and forecast of banks around the world. It, also, analyzes the role of retail banks in economic growth and it provides an in-depth insight concerning the five forces analysis and the customer life-cycle management.

Section 2

Market landscape provides details about the retail banking market segmentation and the top key players. Moreover, this section analyzes the trends that will affect the retail banking sector and it also describes the drivers of change. In addition, it examines the impact of new technologies in retail banks while it evaluates the main and support activities of value chain in retail banking industry.

Section 3

Operating environment examines the pricing policy in retail banking. More precisely, it analyzes the impact of pricing policy on customer satisfaction and it provides an in-depth analysis regarding the pricing policy of different financial products. Furthermore, it presents the business models that are considered to be the most appropriate for retail banks, taking into account the implementation of technology and the latest changes.

Section 4

Competitive landscape records the market share of banks in global level whilst it analyzes the competition in banking sector. Furthermore, it provides details regarding the M&A activity in the global banking sector.

Section 5

Evolving themes examine the workforce trends and employment dynamics of retail banks. More precisely, subjects such as staffing models, staffing systems, education of bank employees and more are analyzed in this section. Also, except for workforce and education, this specific section investigates the digital change in retail banking and the impact of technologies on customer expectations.

Section 6

Shaping the future concludes and recommends the best practices for retail banking. More precisely, this section provides suggestions to retail banks for the adoption of the new trends and the awareness of possible challenges.

Objectives of Market Research Report

This study has assimilated knowledge and insight from business and subject-matter experts, and from a broad spectrum of market initiatives. Building on this research, the objectives of this market research report is to provide actionable intelligence on opportunities alongside the retail banking market size of various segments, as well as fact-based information on key factors influencing the retail banking market-growth drivers, retail banking industry-specific challenges and other critical issues in terms of detailed analysis and impact.The report in its entirety provides a comprehensive overview of the current global condition, as well as notable opportunities and challenges. The analysis reflects latest trends in retail banking, growth drivers, threats and opportunities.

The study addresses retail banking market dynamics in several geographic segments along with market analysis for the current environment and future scenario over the forecast period. The report also segments the retail banking market into various categories based on the product, application and region among others. This analysis also examines the competitive landscape within each market.

Study Scope

PROVIDING AN INDUSTRY OVERVIEW

To succeed in the rapidly changing landscape, banks need to have a clear sense of the posture they wish to adopt-whether to shape the industry, rapidly follow the leaders, or manage defensively, putting off change. Also, they need to have a clear strategy to deal with these challenges and address these priorities, including considering partnerships with third parties and applying lessons from other industries. Of course, the level of focus on each of them depends both on a bank's starting point, and its unique strengths and challenges.

M&A ACTIVITY

Globally, the banking sector appears to have regained its confidence and, with improving macroeconomic indicators, is now pivoting back to a growth agenda which will drive M&A activity.
We review the current M&A activity.

EXPLAINING THE KEY MARKET FACTORS

Powerful forces are transforming the retail banking industry. Growth remains elusive, costs are proving hard to contain and return on equity (ROE) remains stubbornly low. Regulation is impacting business models and economics. Technology is rapidly morphing from an expensive challenge into a potent enabler of both customer experience and effective operations. Moreover, non-traditional players are challenging the established order, leading with customer-centric innovation while new service providers are emerging. Customers are demanding ever higher levels of service and value.

UNDERSTANDING MARKET TRENDS

The pace of change will dictate the emerging structure of the retail banking landscape. Trends such as Artificial Intelligence (AI), open banking, Distributed Ledger Technology, robotic process automation, cyber security, among others, are all important factors that we review.

Note on Research Process & Methodology

Our clients use our insights, critical analysis, statistics and forecasts to help make strategic business decisions and grow their organizations. Our research collection offers unique industry perspective, qualitative and quantitative focus. The quantitative analysis is strengthened by a qualitative assessment, based on a literature review, as a means of exploring and illustrating the present scenario and the growth prospects of the retail banking market. We draw on available data sources and methods to profile developments.

We use computerized data mining methods and analytical techniques, to identify patterns from publicly available online information on enterprise web sites.

Historical, qualitative and quantitative information is obtained principally from confidential and proprietary sources, professional network, annual reports, investor relationship presentations, and expert interviews, about key factors, such as recent trends in industry performance and identify factors underlying those trends-drivers, restraints, opportunities, and challenges influencing the growth of the market, for both, the supply and demand sides.

In addition to our own desk research, various secondary sources, such as World Bank, Statista, are referred to identify key players in the retail banking industry, supply chain and market size, percentage shares, splits, and breakdowns into segments and subsegments with respect to individual growth trends, prospects, and contribution to the total market.

RETAIL BANKING OVERVIEW

SECTION 1

1.1.1 Introduction

Retail banking market is becoming a battleground where competition is getting more and more multifaceted. Retail banks have long competed on distribution, realizing economies of scale through network effects and investments in brand and infrastructure. But even those scale economies had certain size limitations. As a result, in most retail-banking markets, a few large institutions, operating at similar efficiency ratios, dominate market share[1]. Retail banking sector is being transformed by a range of powerful forces.

Regulatory requirements in combination with customer expectations for greater personalization and technological innovation are challenging traditional business and delivery models. To this end, retail banking sector continue to innovate both products and processes in order to remain relevant and to respond in the best way possible in this new operating environment. Since, the customer remains at the centre of banks, innovation efforts should focus on the improvement of digital customer experience across new touch-points and channels. In this context, many banks claim that mobile and online should be the primary distribution channels in the next years. The advent of phone banking and internet banking, however, has expanded the definition of retail banking. Most banks with traditional branches also boast direct phone, mobile and internet banking as additional or alternative services for customers. These can be almost “virtual” banks, but although this increases competition, variety and creativity in the market, they really do nothing fundamentally different from the traditional branch-based banks. Customers in retail banking are able to use local branches of larger commercial banks. Some of the most important products offered by retail banks are fixed, current/savings account on liabilities side; personal loans, house loans, auto loans, and educational loans on the asset side.

[1] *Gujral, V., Malik, N., & Taraporevala, Z., 2019. Rewriting the rules: Succeeding in the new retail banking landscape, McKinsey.*

1.1.2 Definition and Objective of Retail Banking

Retail banking is known as the division of a bank that deals directly with retail customers. Moreover, many times it is referred to as consumer banking or personal banking. Banks that focus on retail clientele are relatively few and most retail banking is conducted by separate divisions of banks, large as well as small. Customer deposits garnered by retail banking represent an extremely important source of funding for most banks[2].

The main objective of retail banks is to collect funds from depositors and lend borrowers. Retail banks are usually defined by the products and financial services they offer to individuals. The most significant functions of retail banking are credit, deposit, and money management. These specific functions can be considered as a component of commercial banking.

More precisely, the function of credit refers to the money that banks lend to consumers to purchase homes, cars, and to cover their personal needs. To this end, retail banks provide money to the public in different ways including inter alia mortgages, auto loans, and credit cards.

In addition, retail banking is considered a safe place where customers feel reassured about depositing their finances. In addition, customers are able to manage their money through checking accounts and debit cards, meaning that customers can exploit online banking to do their transactions with convenience.

[2] *Majaski, C., 2019. Retail Banking vs. Corporate Banking: An Overview*

1.1.3 Characteristics of Retail Banking

Today's retail banking sector is characterized by the following features:

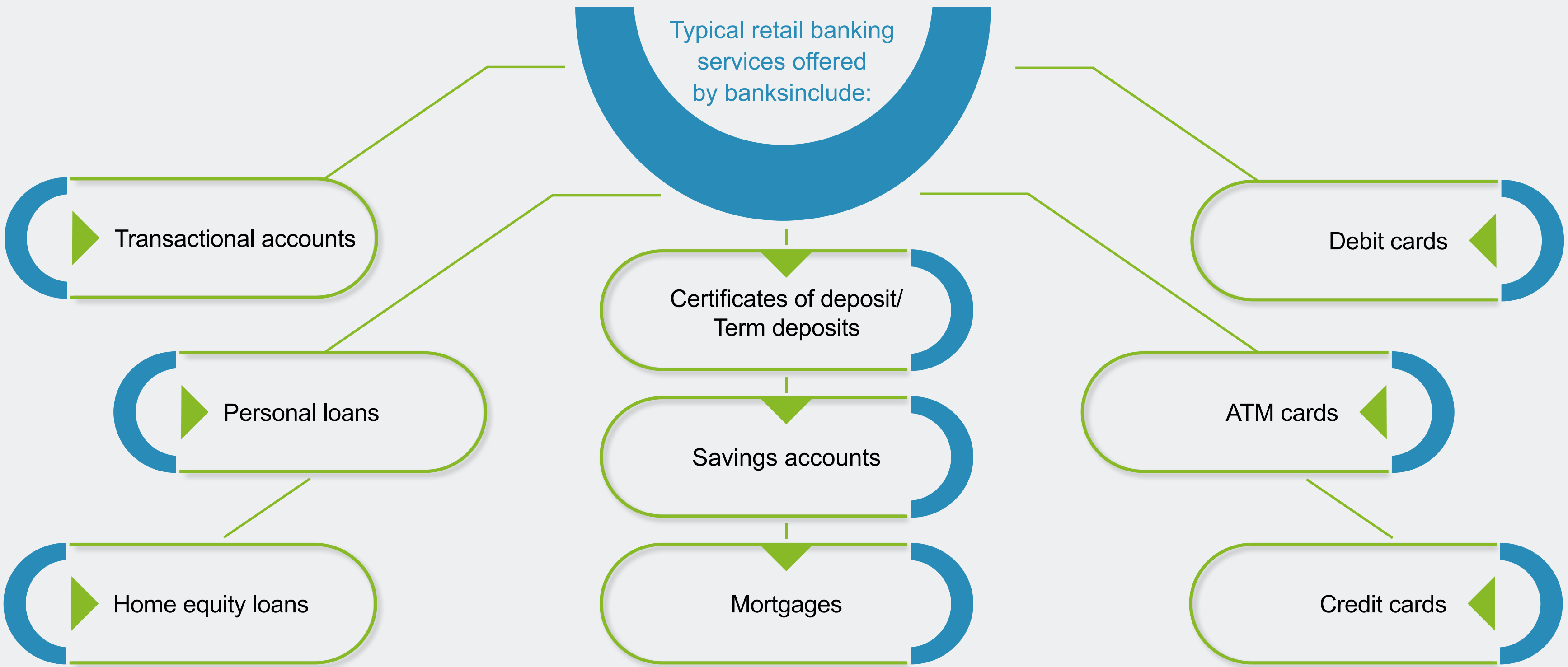
Doing business in large volume of transactions.

The high competition among banks. This could be explained by the large number of retail banking products that are offered by banks and are extremely customer-friendly.

Furthermore, it should be mentioned that in retail banking industry, banks are able to diversify their asset portfolio in order to minimize their risks. For instance, the very low value of loans which are offered to consumers contributes to low probability of default, and hence, reduces the risk of non-performing assets (NPA).

Banks adopt multiple channels of distribution of retail banking products. These channels include inter alia call centre, branch, internet, mobile phones and ATMs. Retail banking is mass market banking, where consumer's individual and diverse needs are fulfilled at a local level. this has been facilitated by the growth of banking technology and the automation of the banking process.

1.1.4 Products and Services of Retail Banking



1.1.5 Supply Chain

Various factors have been discussed which play a key role for the better function of supply chain management in banking sector. These factors are known as supply chain integration.
The overall process of physical and financial supply chain is explained in the figure below.

INFORMATION SHARING

The concept of information sharing in the banking industry also covers the extent to which the relevant and exact information is shared between one supply chain partner to the other. It includes customer orders, scheduling the orders, and enabling private partners to monitor the progress of products and services. Information sharing is considered to be a key indicator in explaining the overall performance of the banks.

CUSTOMER RELATIONSHIP MANAGEMENT

The customer relationship management, or CRM, provides the opportunity for banks to develop a structure in order to manage their bonds with the customers. Moreover, CRM helps the banks discover and identify the needs of their customers in order to appropriately develop their products and services.

CUSTOMER SERVICE MANAGEMENT

The idea of customer service management, or CSM, signifies the service being provided to the customer. CSM deals with the agreements between banks and their customers aiming at satisfying the latter's needs. Different policies have been set in place in order to face customers feedback. Moreover, products and services are improved as a result of effective communication. Thus, the main purpose of the aforementioned management system is the satisfaction of the customer.

CONTROL OF QUALITY

Quality control plays a significant role in the supply chain, as it checks the delivery of the product or service, thus acquiring feedback with regards to the customers' ultimate satisfaction.

CUSTOMER'S DEMAND MANAGEMENT

The concept of demand management entails the process and procedure that create a balance for the customers' demand through business output. Demand management theme captures the demand forecasting.

FLOW MANAGEMENT

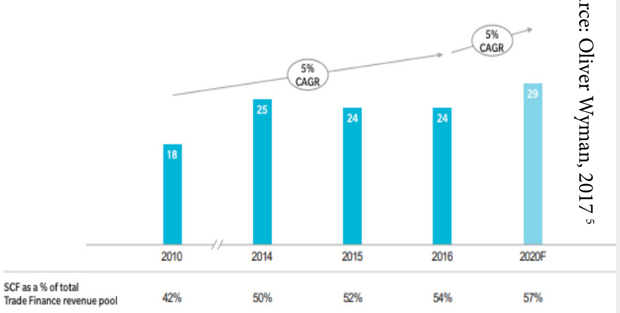
Flow management process is responsible for the actual delivery of the products or services. With regards to retail banks, it should be mentioned that they operate some of the largest, most complex and most secure supply chains in the world, transporting and storing cash across thousands of locations every day. The cost of operating these supply chains extends to expenditures for all the equipment and services required to process and distribute cash throughout the bank's network-from the central bank to branches or ATMs, and ultimately to customers. These costs usually are high and they grow due to two main drivers which are the rising demand for cash and the increasing use of more complex technology across the supply chain.

Anggraini, D., Hamiza, A., Doktoralina, C., & Anah, S., 2018. Application of Supply Chain Management Practices in Banks: Evidence from Indonesia, Int. J Sup. Chain. Mgt, 7 (5).

1.1.5.1 The Rise of Supply Chain Finance

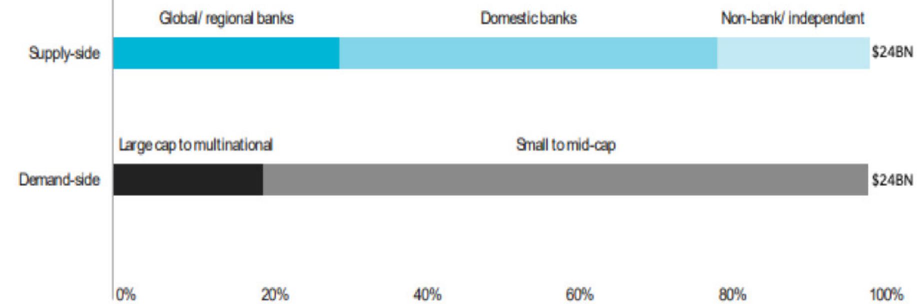
The supply chain finance market grew from 2010 to 2014. More precisely, it has outpaced the traditional trade finance market as the shift to open account trade continues, with the former now representing more than a half of the overall trade finance revenue pool. This shift is driven by maturing trading relationships and better transparency in global supply chains, both of which reduce the need for risk mitigation solutions.

Figure 1.1: Global supply chain finance revenue pools (in USD bn)



Source: Oliver Wyman, 2017 [5]

Figure 1.2: Supply chain finance market structure



Source: Oliver Wyman, 2017 [6]

The need for financing solutions to bridge the gap between orders and the delivery of goods remains, and this demand is increasingly being met by supply chain finance.[4]

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[4] *Sommer, M., & O'Kelly, R., 2017. Supply chain finance: Riding the waves, Oliver Wyman.*

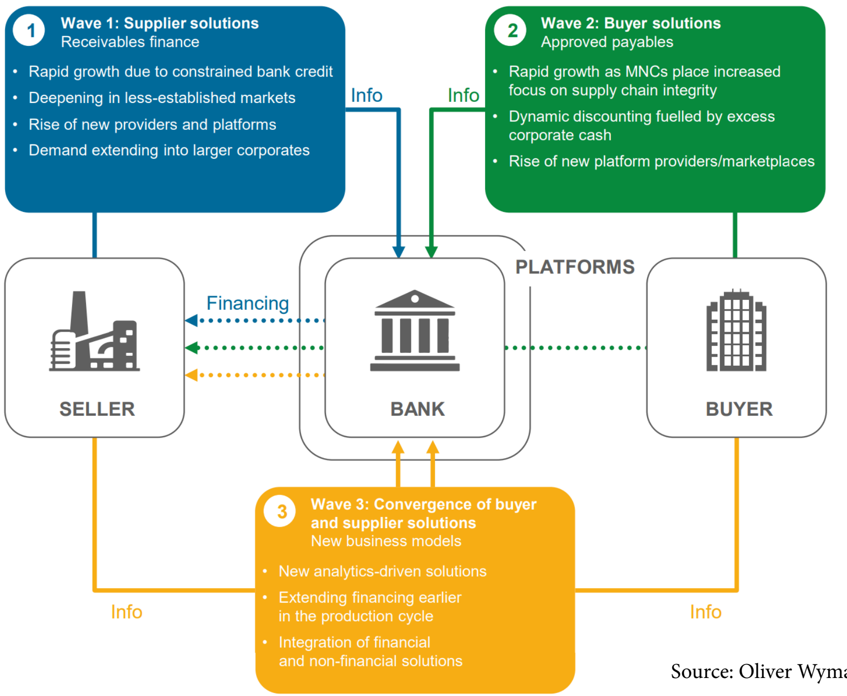
[5] *Sommer, M., & O'Kelly, R., 2017. Supply chain finance: Riding the waves, Oliver Wyman.*

[6] *Sommer, M., & O'Kelly, R., 2017. Supply chain finance: Riding the waves, Oliver Wyman.*

The supply chain finance market is highly fragmented with the largest global and regional transaction banks capturing only around a third of the market. The revenue pool is also skewed towards smaller clients which provide about 80% of total revenues. Smaller clients have traditionally had more limited access to unsecured financing, and the high margins have attracted banks to provide factoring and invoice discounting solutions to meet this need.

It should be noted that over the last decade, traditional trade finance has suffered from increased costs and complexity of providers, because of stricter compliance requirements and the introduction of new capital regulations under Basel II and III. Over the same period, margin pressure has increased significantly due to growing competition. Supply chain finance has developed in three waves beginning with supplier-led solutions, moving to buyer-led solutions, and then, to solutions that combine both of them. Each wave is still advancing and they all offer new opportunities.

Figure 1.3: Three waves of growth



Source: Oliver Wyman, 2017 [7]

[7] *Sommer, M., & O'Kelly, R., 2017. Supply chain finance: Riding the waves, Oliver Wyman.*

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