KPMG

Platform-based banking

Thriving on disruption series

Banks are currently operating in a challenging environment of competitive threats, regulatory pressures, fast-evolving customer preferences and low interest rates. As a result, profitability in the sector has struggled to reach pre-financial crisis levels, with European banks finding it difficult to offer returns to investors above the cost of equity.

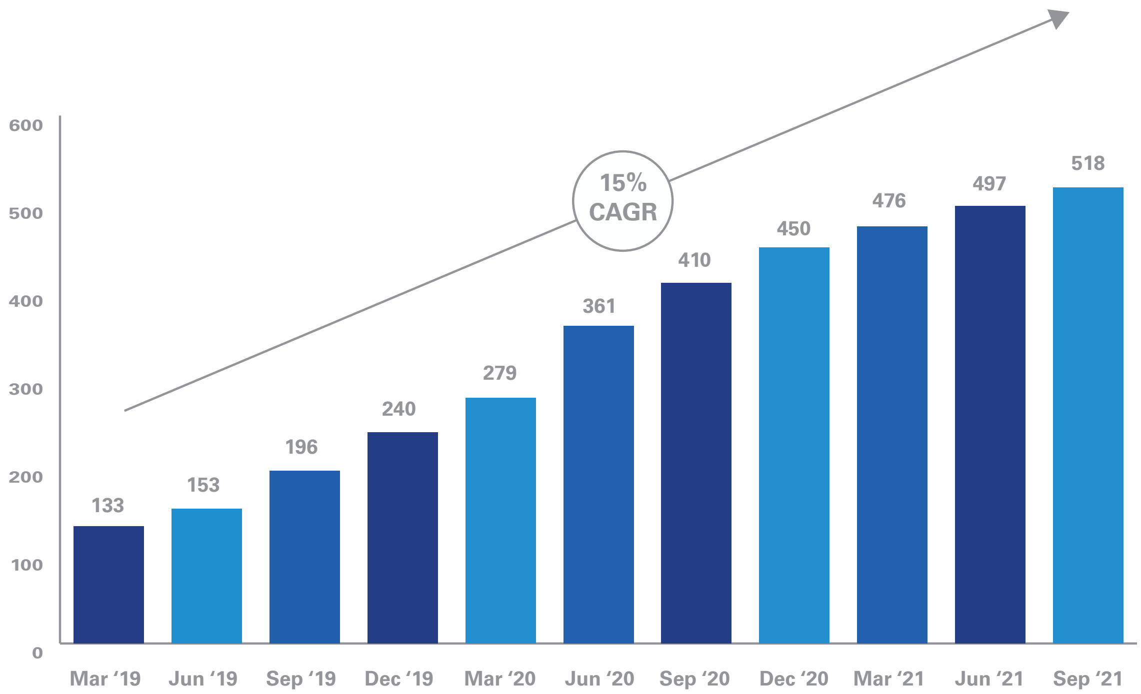
In this difficult climate, platformification offers banks a significant opportunity to create new forms of customer value and open up new avenues for growth. Through platforms, banks can carve out a fresh role as the centre-piece or participant in a digital ecosystem, connecting service providers, Fintechs and customers with monetisation opportunities as the common point of connection.

The platform game

The emergence of the platform business model is a significant feature of modern economies, with examples such as WeChat and Alibaba advertising the enormous benefits available to companies that can manage the transition to this customer-centric approach. Platforms function as digitalised, open, and participative business models that create ecosystems of consumers and producers, united by a set of interaction rules. Because they leverage the production capacities of independent third parties, they often carry no inventory, enabling them to scale rapidly in response to consumer demand.

This trend towards platformification, facilitated by the ubiquity of mobile access, has major implications for legacy banks, since it offers FinTechs and other challengers the opportunity to threaten their vertically integrated and product-focused business model (see Figure 1 outlining the growth in open banking registrations from third party providers for evidence that this is already underway). Whilst all banks have taken steps to digitalise existing business models to some degree, this approach now offers diminishing returns in terms of improved customer experience and cost reduction. In contrast, platformification represents a potential paradigm shift, in which banks can re-invent themselves and their commercial and operating models.

Figure 1: Number of open banking third party registrations in Europe 2019-2021[1]



[1] Source: Konnetex-Mastercard Open Banking Tracker, accessed January 2022

What role can banks play in the platform world?

The threats posed from this new model to banks are clear but legacy players also need to understand their value and grasp the opportunities that platformication offers. However, even though they have access to the same cloud-based technology stacks and rapid-development methodologies as the FinTech innovators, incumbents have been slower to take advantage of these opportunities. In order to do this banks need to move away from their vertically-integrated value chains that stretch from production to sales, distribution and servicing. Possibilities abound for those willing to take the leap.

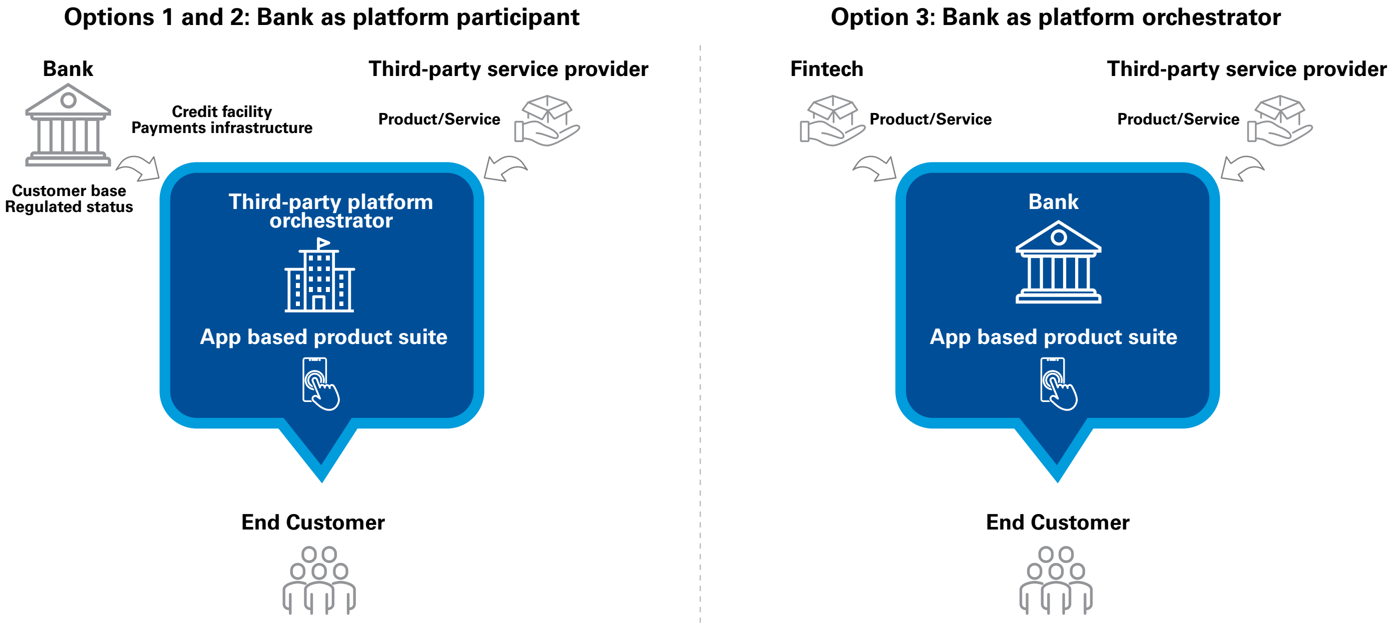
We see 3 broad options:

1. **Limit activity to meeting minimum open banking regulatory requirements.** Banks that adopt this approach and see open banking as a mere compliance issue will miss out on the opportunities that regulation such as PSD2 offers and their return on investment will be limited.

2. **Leverage capability to plug into other platforms as the key provider of financial services.** Banks can play a key role in a range of platform models through the Banking as a Service (BaaS) model by offering their payments infrastructure, funding and customer base to embed finance into third party online applications.

3. **Become the "orchestrator" of an online platform.** This approach enables developers and 3rd party technology firms from FS and adjacent industries to build customer propositions within the bank's IT infrastructure, providing the bank's existing customer base with a wider range of products and services.

Figure 2: Participant vs orchestrator



Opportunities to capitalise

In the context of broad pro-active choices described above (options 2 and 3) we see a range of opportunities for banks, in embedded finance, BaaS, and the rise of super apps.

I. Embedded finance

Embedded finance describes the addition of banking and payments services into the websites and mobile apps of non-bank companies, e.g. payments embedded into a taxi app; flexible finance at the point of sale in online retail; travel insurance offers when booking a flight. This additional offering can have a significant impact on top line revenue growth for companies (e.g. embedding lending at online checkout has been shown to increase purchase conversion by up to 50%), as is evidenced by moves such as Walmart's tie up with FinTech investor Ribbit.

II. BaaS

Banks can act as enablers of embedded finance by offering their payments and banking infrastructure through the so-called BaaS model.

BaaS facilitates fintech companies and other third-party organisations to connect with a bank's system via APIs in order to build innovative financial services upon the provider bank's regulated infrastructure. Financial institutions already offering third-party apps to access customer data include BBVA, Capital One, Citibank, HSBC and Wells Fargo amongst others.

III. Super apps

As customers spend vastly more of their time on digital platforms, banks need a digital platform strategy that reflects their changing demands for new levels of engagement, customisation, and simplicity. Super apps are capturing consumer screen attention more comprehensively than ever before, with successful examples such as WeChat and Alipay becoming deeply embedded in user's day-to-day lives.

Whilst the super app success stories so far have been of Asian origin, the model is gaining traction in the West (and in financial services), with Revolut hoping to build the "world's first truly global financial super app". Revolut offers FX, travel insurance and investment management services in conjunction with their current account offering through a tiered subscription pricing plan. Banks that fail to understand their value proposition in a super app world or fail to execute in a way that delivers on that proposition, risk irrelevance.

Building a platform-based business

Moving towards the delivery of financial services through digital platforms and the construction of an end-to-end customer experience will take a major shift for many industry incumbents. It is important for banks to recognise that the opportunity to provide solutions is not limited to their existing product set, but also those of other third parties. Sharing economic value among participants is critical to the long-term success of a digital platform ecosystem.

Banks wishing to truly embrace platform models will need to re-evaluate the way that they interact with customers. It will no longer be sufficient to take a passive approach and consider the customer's initial touchpoint with the bank as the beginning of a suite of internally focussed customer journeys. Instead, banks should begin by evaluating the customer's entire range of needs (financial and non-financial, existing, and anticipated) and consider in what ways they could meet them via an ecosystem of value-add products. Investment should be focussed on solutions that serve a critical customer need and where banks can provide unique value.

The most challenging aspect of moving to a platform-based approach will be the integration of critical and often siloed elements from strategy through to digital technology. Differences in organisational culture, strategy, and execution requirements mean that traditional "pipes" businesses are not always well suited to launch platforms. With this in mind, banks have a stark choice to make about whether to create their own digital platforms or partner with existing third-party offerings. To be successful, they need to keep in mind a number of lessons, as illustrated through the following case studies.

CASE STUDIES

Singapore – DBS

Think beyond banking needs only - DBS PayLah! (the bank's payments app), allows customers to book a taxi, order lunch or buy tickets for a show through a range of partners and also rewards customers with loyalty points that can be used at a range of outlets.

Innovation isn't just for technologists - 3,000 staff were trained in the fundamentals of AI/machine learning through innovative gamification methods.

Digital platforms can generate meaningful business - ecosystem partnerships with e-commerce, telecommunication and loan aggregator companies contributed more than 30% of unsecured loan volume for almost 20% of new digital accounts in relevant markets and DBS Property and Car Marketplaces generated more than SGD1bn (€650mn) in loans in 2020.

Australia – Commonwealth Bank of Australia (CBA)

Move beyond customer service into building customer experiences - CBA are looking to "build out a shopping experience" through partnerships with third parties such as Little Birdie, the loyalty platform.

Platforms can bring together and benefit the full customer base - the shopping experience platform will act as a large and low-cost lead for business customers, bringing them together with retailers to add value to all customers.

To conclude, some key considerations by market participant type:

Legacy banks

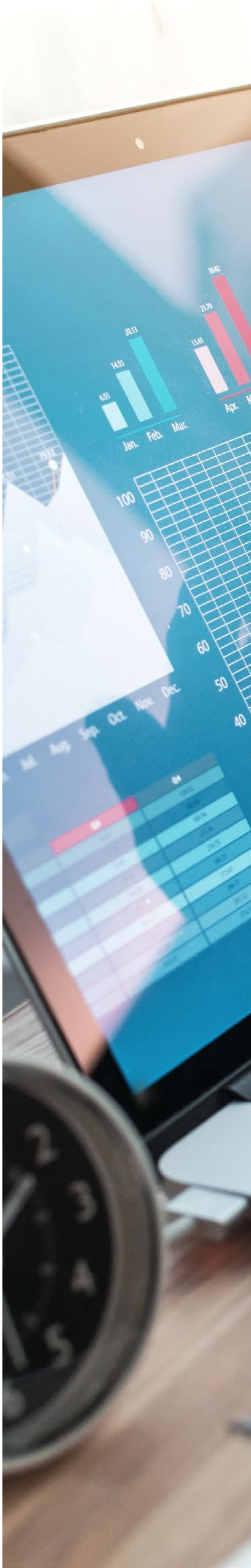
- Ensure that options for platformification are integral to all elements of new strategy development and decide what role to play (orchestrator vs participant)
- Build 3rd party relationships with financial services, and non-financial services partners leveraging strong customer base and balance sheet
- Undertake "blank-page" redesign of the customer experience
- Build up digital expertise across the organisation upgrading data and analytics and automation capabilities
- Reshape the business architecture ensuring easy integration with third party providers
- Get the basics right on digital transformation for cost reduction but don't let that be the sole focus

Neo-banks

- Build value proposition based on addressing customer needs not currently served by traditional players
- Structure platforms to encompass open banking APIs
- Anticipate regulatory challenges - regulator comfort levels with disruptive business models differ significantly by jurisdiction, even within Europe
- Build corporate development capability to enable efficient execution of partnerships and acquisitions
- Leverage smaller size to steal a march on legacy players and innovate at pace

Fintechs

- Experiment with minimum viable product (MVP) and rapid prototyping
- Consider partnerships with larger banks to access new customer pools
- Ensure brand and cultural integrity when partnering with larger players
- Market offering based on its ability to solve customer problems, not its back-end technology
- Don't undersell potential value to larger players and ability to solve the problems they can't

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Contact Us

Christopher Brown
Head of Strategy
KPMG in Ireland
e: christopher.brown@kpmg.ie
t: +353 87 050 4453

Alan Boyne
Head of Transaction Services
KPMG in Ireland
e: alan.boyne@kpmg.ie
t: +353 87 744 2645

Gerard Duffy
Manager, Strategy
KPMG in Ireland
e: gerard.duffy@kpmg.ie
t: +353 87 111 6976

Pablo Montes
Manager, Strategy
KPMG in Ireland
e: pablo.montes@kpmg.ie
t: +353 744 1923

kpmg.ie/strategy

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