



Payment Service Banks

**The 'Challenger' Banks
in Nigeria**

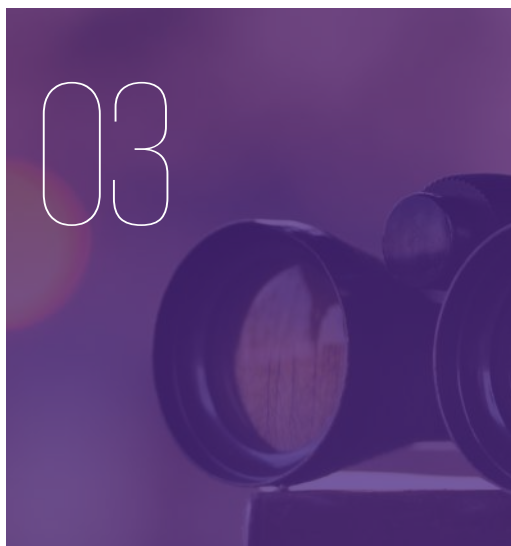
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Foreword

Payments are fundamental to how banks interact with customers. They underpin most propositions and touch customers more than any other part of a bank. It is the key battleground for the customer's primary relationship. Payment Service Banks (PSBs) could revolutionise financial services in Nigeria as they usher in a new era of change in delivering innovative payment solutions to customers across an evolving channel environment.

With several entities signifying their interest to apply for PSB licences, these new entities could become 'challenger banks' as they take on traditional banks in Nigeria. The potential success of these challengers to make inroads in the domain of the strong incumbents, and boost competition in retail banking, will depend on their approach to market and the value propositions they create.

Various market forces are poised to challenge the position of established commercial banks and may shift the balance of power in favour of these challenger banks for selective banking services. PSBs have the potential to be more agile and nimble, and hence more responsive to changing market trends. With few or no legacy constraints and greater responsiveness to customer needs (and with no pressure to offer full-service banking solutions), they may attract a large pool of well-served, underserved as well as unserved customers. PSBs may no doubt find it relatively easier to attract customers, but they still need to identify a profitable pool of customers and monetise these relationships.

While much of the efforts of the incumbent banks may be constrained due to traditional models being expensively built

to last generations, PSBs are anticipated to offer new blood with their innovative models and a fresh 'hi-tech and hi-touch' digital approach.

This publication is an attempt to capture the emerging market trends and their likely strategic implications on the business of these challenger banks. We have made an earnest attempt to identify critical profitability levers for PSBs and have elucidated on how some of these levers can be adjusted to improve profitability, leveraging lessons from India and other climes, and potentially shorten the gestation period. We have also articulated what we believe is the unfinished business on the regulatory front.

We hope that both challengers as well as incumbent banks find this publication useful, as competition and collaboration is inevitable. We at KPMG in Nigeria wish these 'game changers' all the best in their journey.



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Strategic Considerations for PSBs

PSBs to play a key role in promoting financial inclusion in Nigeria

The Central Bank of Nigeria (CBN) recently introduced regulations and guidelines for the licensing and operations of PSBs in the country. This was in furtherance of the apex bank's efforts to leverage technology to promote financial inclusion and enhance access to financial services for the unbanked and underserved segments of the population. The CBN's vision is for 80 per cent of Nigerian adults to be financially included by the year 2020.

According to the CBN, a major objective for the establishment of PSBs is to leverage mobile and digital platforms to enhance financial inclusion in rural areas, especially the underserved parts. This is expected to be achieved by increasing access to deposit products, payments and remittance services to small/micro businesses and low income households.

How PSBs compare with traditional (commercial) banks

Licence Type	Commercial Banks	PSBs
Minimum Capital Requirements	<ul style="list-style-type: none"> Regional Authorisation – ₦10 billion National Authorisation – ₦25 billion International Authorisation – ₦50 billion 	<ul style="list-style-type: none"> ₦5 billion
Permissible Activities	<ul style="list-style-type: none"> Retail and corporate banking services; mortgage inclusive Provide finance and credit facilities Deal in and provide foreign exchange services Settlement bank Issue debit, credit and prepaid cards Undertake fixed income trading 	<ul style="list-style-type: none"> Deposit taking (except public sector) Payments and remittances Issue debit and prepaid cards Operate electronic wallets Invest in federal government and CBN securities Sale of foreign currencies realised from inbound cross-border personal remittances
Operating Requirements	<ul style="list-style-type: none"> In line with the requirements of the various authorisations 	<ul style="list-style-type: none"> At least 25 per cent financial service points in rural areas (as defined by CBN) Deploy ATMs Operate through banking agents in line with the CBN guidelines Establish coordinating centres to superintend the activities of outlets and agents

Entities that are currently eligible to apply for a PSB licence include banking agents, telecommunications companies (telcos), retail chains (such as supermarkets and downstream petroleum players), mobile money operators (MMOs), courier companies, and financial technology (fintech) firms. Switching companies are excluded from owning PSBs to avert any conflict of interest, as they may have access to the data of other operators.

The business of PSBs hinges on providing last mile connectivity and payment facility through either physical points or through other digital interfaces, including mobile or internet-enabled platforms. The last mile connectivity approach can be analogous to an agent banking model with similar operating economics, and mobile-based delivery is akin to mobile banking services offered by banks.

The agent banking approach has had limited success in Nigeria, despite a huge potential, and has suffered challenges around its viability. On the other hand, mobile banking has witnessed significant growth in the last 18 months with the introduction and adoption of USSD and mobile apps. This provides a market entry point for PSBs, as they finalise their business strategies, as they do not have to overcome the barrier of education and adoption of this channel.

In the subsequent sections, we have highlighted strategic considerations for PSBs before they sign-off their strategy and business models and move into operations.

Emergence of two distinctive segments within Nigeria - PSBs can serve both

Besides offering basic deposits and remittance services, PSBs are likely to introduce smooth, real-time, secure, on-the-go approaches for facilitating retail payments. However, the interpretation of these propositions can be very different for two distinct segments of Nigerian consumers as described in our analysis below.

On one hand, the new breed of young, urban and internet savvy consumers are gradually shifting from internet banking and card-based payments to mobile and wallet-based payments to reap the benefits of multichannel, anytime, and any device banking. On the other hand, the rural and low-income consumer segments have limited penetration of basic banking facilities, and hence, limited awareness about how to use banking channels. Expectedly, adoption will depend on how services of PSBs resonate with emerging consumer briefs.

A comparison across these two distinctive consumer segments illustrates a tale of two Nigeria, with different demographics, adoption patterns and challenges, and consequently, different expected propositions from new PSBs.



A tale of two Nigeria

	Banked and technology savvy segment with higher internet penetration	Banked/unbanked/underbanked segment with limited access to internet facilities
Customer demographics	<ul style="list-style-type: none"> • Educated and technology savvy • Average age of 25 – 35 years • Middle/upper middle income segment • Mostly reside in urban, or semi urban areas 	<ul style="list-style-type: none"> • Less educated with limited knowledge of using technology for availing services • Lower middle and lower income segment • Mostly reside in rural and semi-urban areas
Challenges faced in using new payment modes	<ul style="list-style-type: none"> • Slow/limited adoption by the banked, owing to user comfort with internet banking, ATMs/debit cards and card transactions • Lack of standardised and easy-to-use payment services 	<ul style="list-style-type: none"> • Low penetration of internet, ATMs, POS, and other enabling infrastructure • Technology inexperience and literacy constraints • Lack of awareness about electronic and mobile payments • Cash continues to be the sole medium for effecting financial transactions
PSBs potential propositions	<ul style="list-style-type: none"> • Secure and well encrypted payment platform • Standardised services enabled by mobile technology and enriched with data layer (white label apps to facilitate transactions) • More use-cases to provide compelling reasons to use digital payments, especially in Person-to-Person (P2P) and Person-to-Merchant (P2M) transactions • Customised merchant offers based on transaction history – both online and offline • Product add-ons such as cashbacks, discounts and loyalty programmes • Rich and visual tool sets for personal financial management and expense tracking 	<ul style="list-style-type: none"> • Access to basic banking services • Simple and intuitive payment platform with local multilingual interfaces • Often used, especially in Person-to-Government (P2G) and Government-to-Person (G2P) segments • A simple and dedicated domestic remittance platform • Customer education and handholding to drive adoption and facilitate usage • Onboarding of small retail merchants on the mobile payment ecosystem to effect non-cash transactions
New offerings	<ul style="list-style-type: none"> • Digital banking and payment approaches which are smooth, intuitive, functionally rich and support anytime, and any device banking • Strong set of customer incentive pull (loyalty programmes, discounts, cash backs) to drive enrolments and usage • Integration with social media feed that understands and predicts what is needed 	<ul style="list-style-type: none"> • Route the direct benefit transfer through the mobile ecosystem to improve familiarity and adoption • Payment to/from the government on the mobile payment ecosystem (conditional cash transfers, small savings schemes, etc.) • Merchant acquisition services for small retail merchants in rural areas on the mobile payment ecosystem

PSBs have to be digital at core

PSBs are expected to adopt digital strategies to acquire new customers and operate efficiently. However, an incremental approach to digital infrastructure may not yield the expected results, considering the structural constraints that have challenged incumbent banks in Nigeria. Moreover, with only 36 million customers (as at December 2018)¹, from an adult population of over 100 million, there is still a lack of awareness/ use of banking services and limited adoption of technology-enabled banking services in Nigeria.

PSBs have to be designed with a philosophy of 'digital at core' through which not only the front offices (customer touch points) facilitate digital interactions, but the complete banking value chain, including activities such as customer acquisition and onboarding, back-office operations, transaction processing, customer service, management reporting, employee engagement, etc., are also digitally enabled. PSBs can offer a distinct digital experience to customers, only if there is a complete coherence across different functional areas on how these digital interactions will move within the organisation.



Besides, providing revenue push and operational efficiency, digital interactions can also enable PSBs to be more attentive to the needs of their customers. Without digital infrastructure at the core, PSBs may not be able to offer a consistent customer experience, and consequently, may not be able to deepen their customer stickiness.

DBS Bank's digitally driven strategy^{2,3}

DBS, an Asian bank with headquarters in Singapore, is one of the largest banks in Asia by assets. The bank was named the world's best digital bank by Euromoney in 2016. Digital innovation pervades every aspect of the bank – consumer, corporate and SME banking, and even the bank's charitable foundation.

According to the CEO, data is the key to being successful digitally, and to win at digital, a bank has to win at analytics. Thus, the bank uses analytics, with over 400 people in the analytics team, to drive day-to-day decision making and to improve personalisation. Analytics has helped to reduce cash outs at ATMs from every three months to none in 2017 and also helped the bank rise from bottom in customer experience in 2009 to the number one position in 2013.

The bank has used hackathons, human centred design and customer journey thinking to move its marketing efforts from sales to advice in its engagement with customers.

DBS launched Digibank India in 2016, after 15 years of operating a profitable but unscalable traditional banking operation in India with 12 branches and 14,000 customers. Mobile-only, Digibank enables customers to open an account in less than 2 minutes and authenticate their identity by stopping at any one of the extensive network of outlets run by DBS partners including over 500 cafes. The bank has 1.8 million customers as of April 2018 with a goal to reach 5 million in three years.

Leveraging biometrics (from the India government's Aadhaar identification programme) and artificial intelligence (through its partnership with Kasisto, a fintech spinoff from the institute that created Apple's Siri), the bank is able to provide low-cost banking to its customers that it can offer introductory interest rates of 7% and still make a profit.

1 <https://nibss-plc.com.ng/bvn/> accessed on 20 December 2018

2 <https://www.forbes.com/sites/tomgroenfeldt/2018/04/15/going-digital-in-banking-dbs-citi-bbva-ing-lead-the-way/#601c83f95877>, accessed on 11 December 2018

3 <https://www.euromoney.com/article/b12kq6p8mv5rh3/world39s-best-digital-bank-2016-dbs>, accessed on 11 December 2018

Mobile-first models could have an edge

With lower financial spreads, PSBs may not be able to cross-subsidise transactions to the extent that commercial banks can. However, by migrating transactions to platforms with lower operating costs, they can reduce the marginal cost per transaction quite significantly, and thus, remove the need for cross-subsidisation. In a recent KPMG–UBS study on mobile banking trends and their impact on banks⁴, it was highlighted that mobile-based transactions are the most cost-effective as compared to other electronic and physical modes.

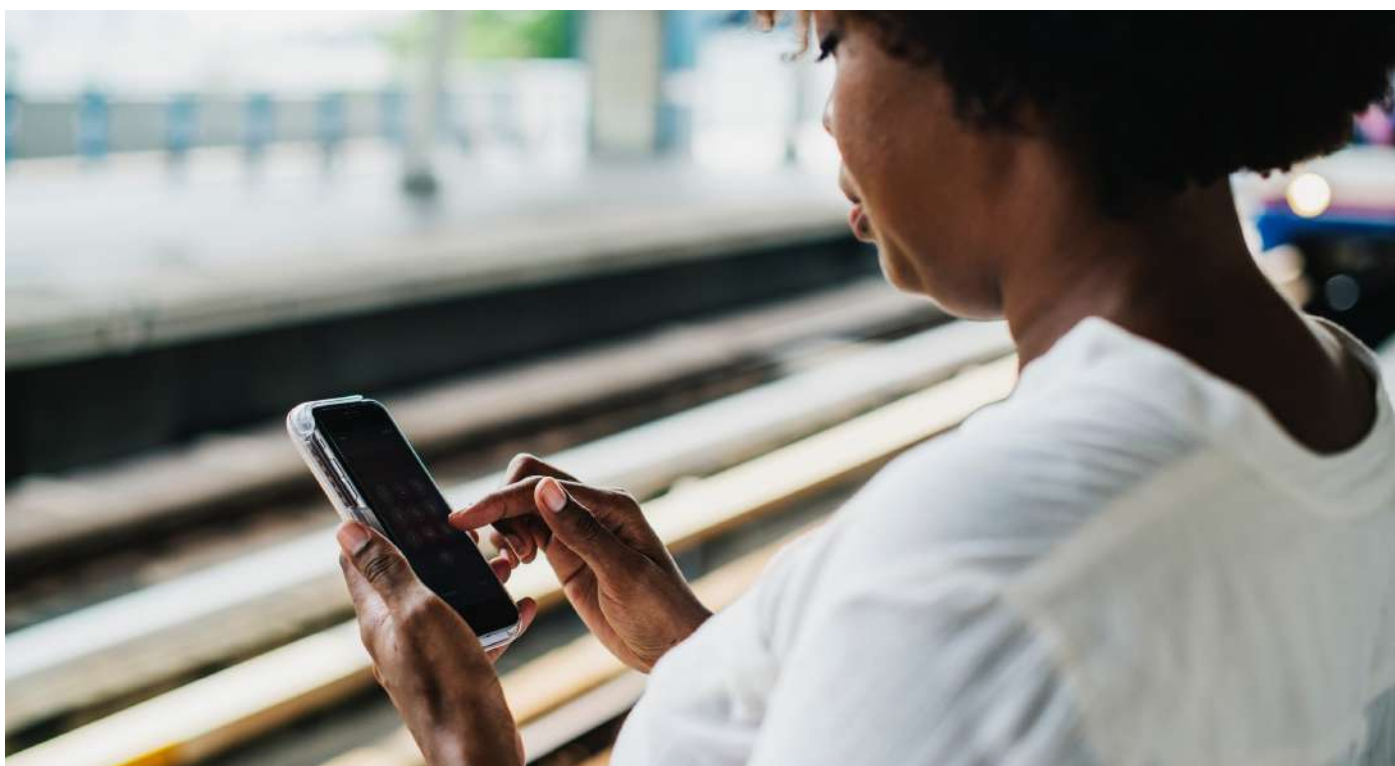
Increasing penetration of smartphones in Nigeria and the popularity of USSD banking, which together made up over 60 per cent of 371 million NIBSS Instant Payment (NIP) transactions in 2017 (estimated to be over 80 percent for the 436 million NIP transactions for 2018 YTD as at August)⁵, is expected to remove some of the bottlenecks that have constrained adoption till now. With more intuitive interfaces and less complex payer procedures, a mobile-based transaction platform has become a major driver of growth for traditional banks and should be a starting point for a PSB.

It is important to note that the partnership model between financial institutions and telcos for the USSD platform still requires further refinement. This is required to ensure that it is a win-win and sustainable relationship for all parties involved, while delivering a seamless customer experience.

Physical branches need to complement digital banking

Digital banking is definitely the future of the industry, but the need of the hour is to introduce and induct the larger Nigerian population of first-time users to the world of technology-enabled banking services. This would require handholding and service assistance through physical interactions, and hence, physical presence in some form. The CBN does not envisage PSBs as branchless banks for precisely some of these reasons. Moreover, as per the final guidelines, PSBs are also required to have at least 25 per cent of physical access points in rural centres. New PSBs could potentially face significant challenges in setting up infrastructure in rural areas, further placing pressure on profit margins.

We believe that the manifestation of CBN's requirement of physical branches could be very different for PSBs. They can augment their reach through merchant networks, as well as introduce 'lean branches' to manage operational costs, particularly in the hinterlands. We also believe that the approach for urban areas could be different and that PSBs may introduce experiential banking through e-lobbies and customer hang-outs. These branches are expected to act as service stations along with showcasing products, and could be designed to enhance the brand appeal of the PSBs.



⁴ <https://home.kpmg.com/content/dam/kpmg/pdf/2015/08/mobile-banking-report-2015.pdf>, accessed on 10 December 2018

⁵ CBN Payment Systems Statistics accessed on 10 December 2018; KPMG Analysis

Merchant acquisition to be as central as adding new customers

Merchant acquiring will not just be an ancillary business for PSBs as it seems pivotal for its success. The much desired network effect for the transaction platform will only kick in when there is an adequate base of merchants and users on either side of the transaction. Moreover, PSBs will have to target merchants across categories, geographies, and in both offline and online categories. They could potentially provide tailored services and innovative ways to structure rates depending on the customer profile, transaction volumes, merchant campaigns, etc. Similarly, onboarding micro-merchants through innovative and other low-cost infrastructure could be a differentiator.

PSBs also have to offer value added services to merchants where they not only facilitate merchant payments, but also help them generate more business by connecting them to the customers or make them more efficient by providing additional business services. To illustrate, consider this example, where a PSB offers a free white label app for small restaurants that can be customised and used for taking and processing customer orders on a tablet or smartphone. This app can also connect to the payment platform offered by the PSB at the back-end, and can further ease out the bill generation and payment processing for the restaurateur.

The new definition of KYC for PSBs

Traditionally, banks started collecting customer information with the introduction of Know Your Customer (KYC) regulations to deter fraud and money laundering and to ensure compliance. However, KYC for PSBs will not be limited to just verifying the identity of a particular customer (at a minimum, as required for Tier 1 accounts), they will have to continually adopt innovative approaches for truly knowing their customer's expectations through their habits, purchase patterns, and online activity. PSBs will have to add a layer of analytics around the Customer Information Record (CIR) that dynamically processes past transactions data, call history, as well as additional data shared by customers, including social media activity data.

Beyond compliance, this information can also provide insights that can help PSBs to customise offerings and also make sure that their communication is targeted at the customer in an effective manner, thereby improving this engagement. Of course, all these activities will have to be done by maintaining customer privacy and taking adequate consent at all times.

Fidor Bank - banking with friends model

Fidor Bank AG, based in Munich, Germany has pioneered its business model on deepening its relationships with digitally savvy consumers and business customers with its Fidor Community. The Fidor Community has become an active financial community, unique in itself, with over 470,000 users engaged in discussions around the clock.

Fidor's motto is 'Banking with friends' and its desires is for the community to advise each other, help increase financial literacy, invest and get help from the community with crowd

funding, bitcoin trading and more. This is borne out of the bank's belief in openness and involving customers in the decision-making process and realisation that people are more likely to go to their friends for financial advice than their banks.

The bank keeps the community active by providing rewards to members who advise their peers, transfer their salary or recommend someone. Financial bonuses can be converted to cash.



Country Insight: India's Payments Banks Experience⁷

The Reserve Bank of India (RBI) granted eleven applicants in-principle approval to set up payments banks in 2015. Seven of the eleven applicants (out of which three are the largest telecom operators in the country) have launched a payments bank. Among the remaining four organisations, three have already surrendered their licences with doubts over the business model viability and the remaining player (Vodafone, a telecom operator) is also most likely to surrender its licence post its merger with Idea (a telecom operator and also a payments bank).

Three of the seven payments banks to launch – Airtel, Paytm and Fino, have been in operations for more than a year. The remaining four started commercial operations only in mid-2018.

How India's Payments Banks have fared so far

Payments banks can only accept deposits of up to INR 100,000 (USD 1,456) per individual customer and are not allowed to lend. This has so far resulted in limited impact with the total deposits in payments banks being less than 0.005% (USD 0.16 trillion) of overall bank deposits. Also, all three major payments banks who have been in operation for over one year have faced challenges in terms of regulatory bans on accepting new customers, imposition of penalties and delayed launches that have impacted revenues and profitability.

In August 2018, the three payments banks to first begin operations recorded a combined 2.15 million debit card transactions. One of the payments banks outperformed all small finance banks and some foreign banks such as HSBC and DBS in terms of number of debit card transactions.

Unlike traditional banks, to expand customer outreach, payments banks have focused on establishing access points rather than a full-fledged branch. To establish access points, they have partnered with retail outlets and small merchants, which has thus enabled them to perform almost all transactions possible at the branch. Airtel Payments Bank, backed by the largest telecom service provider in India, has established over 250,000 access points commensurate to the network of some of the large traditional banks.

Traditional banks have responded to the emergence of Payments Banks

The basic premise of the introduction of payments banks was to increase penetration in the unbanked and underbanked population. As such, their offerings are niche and they are not allowed to provide the entire gamut of banking services, such as asset products and fixed deposits. Thus, the situation still provides traditional banks with significant headroom for growth and also an opportunity to partner with payments banks to offer their products to an unexplored customer segment.

Investment in the payments bank: Some of the large traditional banks have become strategic investors in payments banks. Three of the seven payments banks that have commenced operations received significant investments from some of the biggest banks. State Bank of India (the biggest public sector bank), ICICI Bank and Kotak Bank (two of the largest private sector banks) have investments in payments banks.

Partnerships with payments banks: Since payments banks are not allowed to hold deposits in excess of approximately USD 1,456 per customer or give loans, traditional banks are partnering with payments banks to provide such customers a wider offering including fixed deposits, loans, etc.

For example, IndusInd, a large private sector bank, has partnered with Paytm Payments Bank to channel balances in excess of the above maximum limit as fixed deposits. Fino Payments Bank cross-sells loans on behalf of ICICI Bank.

Tie-ups with digital payment firms: Traditional banks are entering into partnerships with digital payment service providers and fintech firms to offer their products and enhance the online payment experience. For instance, HDFC has tied up with Paypal to enable faster merchant payment and with GooglePay to offer loans.

Regulation has evolved with the market

For example, in the initial guidelines, RBI allowed payments bank to obtain KYC from a telecom company, if such company is a promoter/promoter group entity of the payments bank. During one of the regulatory audits, the regulator observed that Airtel Payments Bank (the first to start operations) allegedly opened accounts of its mobile subscribers without their consent. Subsequently, the regulator toughened its stance mandating that reliance on KYC done by the telecom company is not permissible for opening an account.

As highlighted earlier, three of the major payments banks have faced regulatory bans on accepting new customers, and had penalties imposed on them.



The Winning PSB: Levers for Success

While there is limited evidence to conclude on the economic viability of PSBs or other payments banks, such banks are entering the market with clear advantages given the potential differences in the business and operating model of PSBs. PSBs are expected to develop new capabilities and infrastructure with a legacy-free channel, information technology and application. Moreover, PSBs are expected to operate on an asset-light premise compared to the traditional branch-based and asset-heavy model, prevalent with traditional banks in Nigeria.

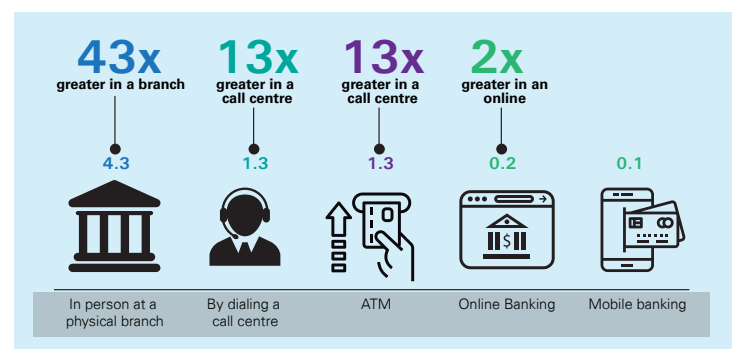
Consequently, the customer acquisition and servicing cost structures of PSBs will need to be different in comparison to a traditional bank. We expect that for the first three to five years, servicing costs of the PSBs will be lower and their customer acquisition costs may be higher than incumbent banks. So, along with keeping the thrust on transaction volumes, PSBs could also manage the levers of servicing and acquisition costs to further improve profitability, as described below.

Lower servicing cost

Profitability of PSBs is expected to be highly sensitive to transaction volumes and gaining critical mass of customers; however, the channel mix through which these transactions will be effected can also have a significant bearing on the overall profitability.

PSBs should aim to push adoption of lower cost digital channels right from the start of their banking relationships. Findings from the KPMG–UBS study indicated that the cost of effecting a transaction from a branch is 43 times, call-centre and ATM is 13 times, and internet banking is twice greater when compared to mobile transactions.

A comparison of customer servicing costs across various channels vis-à-vis the mobile channel



Sources: Javelin Strategy and Research, 2013; KPMG analysis

Consequently, PSBs are expected to promote and incentivise adoption and usage of mobile and digital channels to all customer segments. Evidence from the annual KPMG in Nigeria's banking industry customer satisfaction survey (BICSS) suggests that this will be a viable strategy for PSBs. The findings from the research show that adoption rates for retail banking customers for app-based mobile banking and USSD channels rose significantly from 48 per cent and 41 per cent in 2017 to 55 per cent and 59 per cent in 2018, respectively.

Roll out economically sustainable access points

One of the critical financial inclusion objectives is to increase the number of financial access points. This is very important to facilitate Cash-in and Cash-out (CICO) for customers especially at rural and semi-rural areas of Nigeria. Therefore, achieving a reasonable customer to access point ratio is a critical determinant of customer enrolment and transaction acquisition.

Furthermore, PSBs must also achieve a reasonable balance between traditional branches and using agents as access points. This will largely be driven

by the business model adopted and the need to optimise the cost-to-serve with maximising footprints.

Successful PSBs will need to develop a strategic framework for access point roll-out leveraging analytics and using multiple data sources to make decisions on access point types (agent, branches, coordinating centres, ATMs, etc.), locations, and product suite.

A profitable access point roll-out strategy must encompass:

- **Agent/branch economics:** This will include ensuring that the agents/branches achieve sufficient transaction volume across key products line (CICO, payments, remittances, etc.) while minimising transaction costs (cost of operations, cost of float and liquidity management etc.) to drive economically sustainable agents/branches.
- **Geographic and infrastructure complexity:** Given CBN's requirement of minimum access points of 25% in rural areas, this must account for significant variation factors at various locations including market conditions (e.g. local population, financial transactions dynamics, nature of economic activities), physical infrastructure (e.g. access to electricity, access to mobile networks), operational risks (e.g. security, theft), proximity to financial infrastructure (e.g. commercial banks, microfinance banks).

- **Agent churn and cannibalisation:** This must factor in the challenge posed by competitors (PSBs, incumbent MMOs, etc.) and industry initiatives such as the Shared Agent Network Expansion Facility (SANEF).

Capture transactions

Transactions are anticipated to be the holy grail for PSBs and their build-up will be due to the combined effect of new customer enrolments and the adoption of relevant use cases by customers. Our hypothesis is that a few of these emergent PSBs are likely to have a significant pool of captive customer base when they start operations. These players may be in a situation where customer enrolment may not be as critical a driver for them. It is the adoption of use cases that will be critical to drive transaction volumes.

Based on our analysis of the payments banks experience in India, telcos, despite their large captive customers, have faced challenges to drive adoption and usage due to limited use cases. Lack of cash-out options have also posed significant challenges in the past.

Furthermore, to build competitive advantage through these use cases, PSBs may have to forge alliances and exclusive partnerships with government agencies, large merchants, etc. A robust customer use case mapping has to be designed based on the unique needs of the identified customer segments, which may help PSBs to target specific segments more effectively.

Fino – Banking beyond branches – “Bank in a box”

Fino Paytech is a payment technology solution and business correspondent service provider to banks and financial institutions in India and has been operating in this area for over a decade. It is currently servicing over 28 million active banking customers. It provides a range of financial services like direct benefit and domestic money transfer services largely to the unbanked and unserved segments of the population.

Fino moved ahead in the value chain and launched a payments bank in 2018 with around 400 branches and 25,000 merchant points (banking agents). The bank's focus

is on providing services digitally to remove dependency on branches whilst still keeping the human touch. It equips local merchants with mPOS devices, enabling them to provide services to their customers on the bank's behalf while continuing with their current business seamlessly. The mPOS device, popularised as “Bank in a Box”, uses an android based platform and includes a biometric scanner, PIN pad and card reader. The device enables the merchant to provide the entire bouquet of services offered at a branch ranging from account opening, deposits to purchase of third party products like insurance.

Leveraging its existing presence and focus on a technology-enabled business model, Fino Payment Bank has, within one year of launch, acquired over 1 million customers with approximately USD5 million in deposits. It currently processes approximately USD14 million worth of transactions on a daily basis. It is planning to increase the customer base to 3 million and daily transaction processing to approximately USD28 million by March 2019.

Leverage existing capabilities and infrastructure

A number of the successful PSB applicants will start with existing infrastructure and capabilities that can be harnessed as they set up the business. Depending on the business model, PSBs can leverage the following set of capabilities, among others, as they embark on operationalisation:

- Distribution footprint: physical footprints, established route-to-market (RTM) capabilities, mobile app platform for eWallets, etc.
- Large captive customer base.
- Existing ecosystem for sales and service: agents, distributors, etc.
- Regulation and compliance skills/'know how'.

Partner and complement

While entrants into the PSB space may leverage existing assets and capabilities within their parent network on a fair basis, building robust external partnerships and ecosystems will differentiate the leaders in this space. PSBs must work with relevant external partners that have capabilities in key areas where it may take time to build internal capabilities or where it is not economically attractive to do so.

Potential areas for partnership, depending on the internal capabilities of the relevant PSBs, include:

- Market: e.g. partnerships with specific retailers to offer products, promotions, and gift cards, to create new market opportunities.
- Access Points: partners that can create access points for PSBs including fast moving consumer goods (FMCG) companies and their distributors, downstream petroleum players, etc.
- Processing (cash and liquidity): partners that can assist in cash and liquidity management.
- Technology: partnership with fintech innovators and transaction infrastructure providers to leverage capabilities to share in revenue producing opportunities that concurrently provide an enhanced customer experience.



The Way Forward



Nine considerations before setting up a PSB

Based on our experience in helping banks, aspiring PSBs and broader financial services players set up their businesses and grow, we have distilled our top nine considerations as follows:

Protect the core and ring-fence the PSB build-up

Just as retaining existing customers will be as crucial as acquiring new ones, protecting business as usual will be as important as creating a sustainable banking franchise. Managing this transition with minimal disruption to existing businesses, and at the same time leveraging all the strength of existing businesses will be crucial in defining success.

Reassess and revalidate business strategy

Strategies developed during a limited time frame provided during the application, will require revalidation and, if necessary, redesigned to deepen business models. Newer value chains around the e-commerce ecosystem, rural-urban corridors, MSMEs, etc. are emerging, which could have significant implications on business models. Flexible cost structures have also been evolving to significantly bring down the marginal cost of acquiring and servicing customers.

Build capabilities - digital at the core, human touch at the fore

Given the considerations of the Nigerian market place as well as customer dynamics, there needs to be a human element to the customer interface, even as the entire ecosystem needs to be digital. The interface could be voice, video or face-to-face but there is a need for a more human experience for better customer connectivity.

Analytics to provide once in a generation opportunity to create a customer-relevant business platform

Data driven decision-making is likely to be a digital differentiator. Investments in data analytics platforms will enable PSBs harness the power of predictive data and intelligence to provide insights on customer preferences and enable a more appealing approach to engage with customers.

'Frugal' innovation

PSBs can innovate by reusing existing infrastructure, skill sets, networks and technologies to jumpstart some of the operationalisation activities. The pace of change in technology and the opportunities it offers are extremely dynamic. PSBs could set the pace and industry standards on innovation, and hence, being nimble around operating models is crucial.

No single window for regulatory approvals for operationalisation

This will require proactive management of multiple stakeholders, from getting the business structure aligned to the CBN guidelines, ensuring that regulatory milestones are met in a time bound manner.

Growth, competition and customer demand are likely to foster collaboration and uncommon alliances

The need to address customer life cycle requirements may require alliances with traditional banks and other incumbents or even challengers; identifying the right partners with complementary skills could also be a differentiator.

FYC is the new KYC

Follow your customer will be as important in creating meaningful customer interactions as KYC is from regulatory and business considerations.

Customer likely to be driven by value and not necessarily by price

If banking services are taken as an example, as evidenced from KPMG's decade of customer satisfaction research in Nigeria, cost differentiation is unlikely to be a compelling customer proposition, as would be service and experience differentiation.

The emerging landscape

As PSBs commence their application process, incumbent banks are already investing in and getting ready for the retail onslaught likely to be unleashed by these challengers. However, re-deconstructing legacy technology building blocks, data warehouses and creating their digital presence across channels is going to be time-consuming. So, there is this initial advantage that the challengers have in

creating a perceived edge over the incumbents and carry it over to the next decade.

PSBs are likely to challenge the incumbents primarily on higher customer engagement, coupled with smooth transaction capabilities and volume-driven metrics. To summarise, PSBs are likely to follow the new 6Cs of banking, which can differentiate them from their incumbents.

New 6Cs for PSBs

	Payments banks	Commercial banks
Customers	Higher customer engagement	
Channels		Branches
Culture	alternative innovative collective new enterprising dynamic interesting different	corporate rigid bureaucracy official structure tradition governance workforce
Costs		
Capital		Capital Intensive
Collaboration	Many	Few

Source: KPMG analysis

In Summary

PSBs need to leverage customer analytics to drive contextual insights and experiences, and create stickiness which will be difficult to replicate and break. By offering location-based services, behavioural offers, customised solutions (which open a 'secret window of opportunity'), and non-financial interactions, transactional activity will be relegated to a by-product of a broader customer experience. In fact, challengers will need to become the friend-in-need that follows the daily rhythm of the customers.

Variable costing models will allow challengers to invest in creating a truly omni-channel experience, which will take PSBs to their customers. On-the-go banking – mobile and human handheld devices – are expected to reduce the differentiation between self-service and full service, while providing a smooth customer experience across multiple channels. The challengers could have the design advantage, with no legacy concerns, to build omni-channel capabilities that are fully integrated with the middle and back-end support systems to drive customer value.

While all the emerging PSB entrants will get categorised as challengers, in reality, considering

their pedigrees, most of them are likely to be very different from one another; as seen in the evolution of the banking industry after the 2005 consolidation exercise, some will survive and flourish, while a few are likely to end up being forced into mergers. It will mean survival, struggle, growth and finding the next platform with the focus on value creation at all times.

On a final note, we believe that there is unfinished business with respect to the regulations for PSBs. We believe that the CBN will need to provide further clarity in subsequent guidelines in certain areas, including:

- The definition of what constitutes financial access points for PSBs.
- The ability of PSBs to leverage their platforms for third party financial products, which could further drive the implementation of the apex bank's financial inclusion agenda.
- The sufficiency of the requirement for 25 per cent of PSBs' financial access points in the rural areas, given the CBN's 2020 financial inclusion objectives.
- Guidelines on shared services for PSBs and their parent companies, where such relationships exist.

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