DEAL ADVISORY

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A VIEW FROM

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INORGANIC INNOVATION

There is an exciting new paradigm for financial institutions and corporate development strategists. It is shaped by the acceleration of mega trends, evidenced by seismic shifts in technology, social values, demographics and the environment. Additionally, we are seeing financial technology (FinTech) challengers enter the market, eating away at traditional business models for banks, insurers and wealth managers. Each of these factors is impacting the financial services industry and the real economy it exists to serve, creating disruption and opportunity.

There are plenty of examples of this: Kenya's mobile financial services industry, which underpins up to 60 percent of the country's GDP, is creating a more competitive landscape.[1] Then there is Alibaba in China which is piloting algorithmic credit scoring as well as telematics car insurance in the UK.

There are also evolving stakeholder expectations. In the last 12 months, digital innovation has risen to the top of the corporate agenda. Institutional investors are expecting transformation in this space and many are expecting to factor a company's data and analytics strategy into its investment decisions and company valuation[2]. Furthermore, governments are looking closely at responsible financial services, recognizing the opportunity for financial institutions to promote inclusive and responsible development in both mature and developing economies.

To respond to such changing dynamics, many financial institutions are leveraging external partnerships to innovate more quickly.

KPMG
cutting through complexity

GROWTH OF THE EXTERNAL ECOSYSTEM

Historically, financial institutions have been very private, internalizing all their innovation and development. There is now recognition that this cannot continue. There are too many conflicting internal priorities and bank culture does not typically encourage sufficient experimentation and "safe failure."

Instead, they are looking for ideas externally, using a global ecosystem to help them source leap-frogging ideas, technologies, business models, and in a number of cases, talent. We have seen financial institutions engage in an increasing number of external partnerships with incubators, research institutes, universities, FinTech, telco, governments, customer groups, external consultants, and indeed, with each other. The nature of these relationships is unique to each organization, depending on their objectives.

There are a number of examples, including:

- AIA, a major insurer in Asia, has partnered with KPMG China and Nest, an innovation accelerator platform in Hong Kong, to support wearable healthcare technologies and predictive analytics, recognizing the convergence between the world of health, quality of life and the role insurance can play.[3]

- The Citi Innovation Lab in Singapore, a partnership between Citi, the National University of Singapore and Infocomm Development Authority of Singapore, uses new web, mobile, supply chain and analytics technologies to engage institutional clients to co-create the most effective solutions and products for their business.[4]

- The Commonwealth Bank of Australia recently acquired Tyme, a digital mobile technology firm from Africa as a way to externally source best-in-class leading edge technologies from high growth markets to deploy across its Asia Pacific businesses.[5]

- UBS opened an innovation lab at Level39, a government-sponsored FinTech hub in London. The lab will bring together experts from UBS and the wider FinTech community to create solutions that could have industry-wide significance in managing and analyzing vast amounts of data, and evaluating risk.[6]

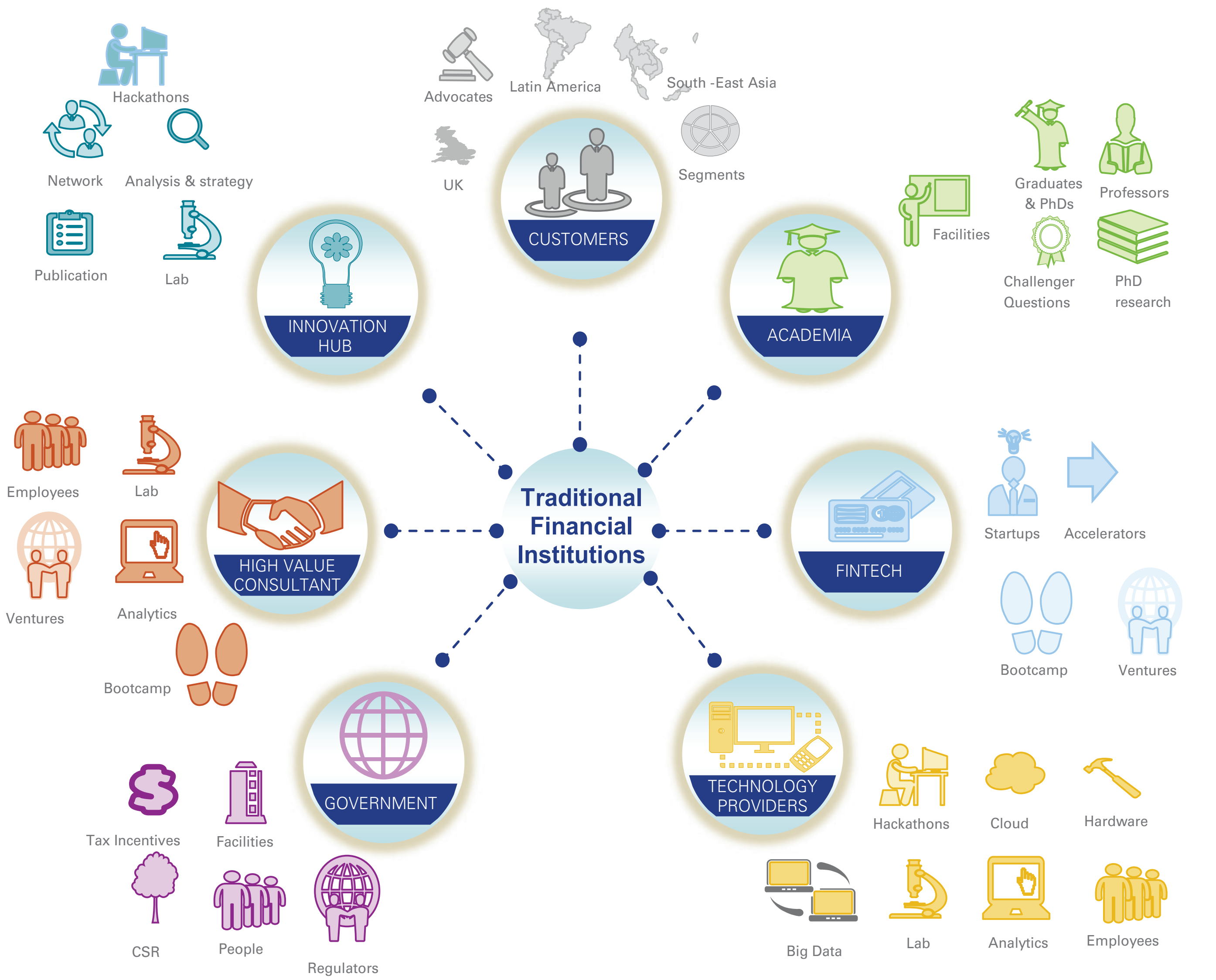
- The JPMorgan Chase Innovation Center at the University of Delaware, which opened in October 2011, works on joint projects with the university's Institute for Business Analytics that focuses on the analysis and optimization of processes in financial services.[7]

> "Cloud-based services are transforming the way corporates interact with financial services providers. We have made an investment into Kyriba so we can better understand and develop our connectivity to future cloud-based systems that our clients are going to use"
>
> – **Christophe Chazot**
> HSBC Group Head of Innovation[8]

Figure 1: Common external partnerships and collaborators

External party	Key features
Customers	Provides focus on customer pain points, identifies new channels to market for B2B2C opportunities. May be engaged through advocacy programs and crowd sourcing rather than more formal joint ventures and alliances.
Academia	Access to academic research, resources for co-development and a presence on campus to support recruitment and brand awareness.
Technology providers	Specialist expertise, access to the latest technological developments and potentially a broader network through collaboration.
Government	Access to national schemes and incentives, and helps organizations take a proactive approach to the regulatory agenda in a rapidly transforming financial services landscape.
High value consultants	Specialist expertise, independent perspectives/challenges, advice on innovation sourcing and broader networks through collaboration.
Innovation clusters/ FinTech	Proximity to new ideas/innovation, access to a network of networks and brand awareness. Helps encourage a more agile and entrepreneurial culture.

Illustrative External Ecosystem



KEY QUESTIONS

As financial institutions consider external ideation, they commonly ask three key sets of questions:

- **Customer perspective:** How will these mega trends impact my customers and their customers? How are my customers innovating to change their business models to capture the opportunity? How can I co-ideate and co-create with my customers and their customers?
- **External engagement model:** What is the right external partnership model for me? Joint venture, alliances, partnerships, acquisition of a majority/minority stake? How formalized does it need to be in quick moving environments? Should I establish a corporate venturing fund? How can I identify and prioritize the right partners?
- **Internal deployment and scale:** Having identified the right innovative ideas and had a successful MVP, how do I scale-up across the business to maximize the benefits and synergies?

SEIZING THE OPPORTUNITIES

Innovation can offer incredible rewards. From new products and services to new digital business models, organizations can enhance the customer experience, retain customers and attract new ones, while simultaneously reducing costs to serve and improve risk management. Organizations can work on their own innovations, but looking to the global market for innovation can enrich what it has to offer in the longer term.

We are already seeing many forward-looking institutions proactively seize the opportunity to source innovation inorganically – and as they do so, they are creating a vibrant external ecosystem that is accelerating the transformation of the financial services sector.

Wei Ng is the High Growth Markets and Innovation Lead for the Office of the Financial Services Chairman at KPMG International.

Sources

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Credits

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