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KPMG Perspectives

Dynamic new partnerships and initiatives are 'at the heart of the digital future' for banks

Part 1

BANKS and financial institutions are globally facing immense challenges as disruptive change—driven by a combination of heightened regulation, fast-paced technological innovation and evolving consumer behavior—reshapes traditional ways of doing business. But banks navigating the transformation trail are struggling in a low-growth economy, balancing financial returns over the short to medium term, while simultaneously investing in their digital capabilities and innovation to position themselves for long-term growth.

Complicating the challenge to innovate more rapidly and efficiently is the complexity of legacy banking infrastructure, the size of organizations and their "risk averse" cultures and hierarchical structures, which often kill innovations before they can gain any momentum.

There's no doubt that new entrants, such as fintechs and, increasingly, e-commerce giants, are bringing fresh and innovative ideas and services to a marketplace of eager consumers who are voicing less trust in—and loyalty to—traditional institutions. A postglobal financial crisis world has seen a transition from the battle of the balance sheet to an intense and urgent new battle to attract and retain customers in today's increasingly competitive environment.

Invariably, every strategy and change initiative will require very careful consideration of these significant challenges in order for such large, complex, highly regulated organizations employing hundreds of thousands of people to truly reinvent themselves amid disruption of the entire ecosystems in which they operate," says Ian Pollari, global coleader, KPMG fintech practice.

"It raises questions about the role of innovative new partnerships and sourcing of new capabilities, and where to invest in and/or acquire fintechs or smaller tech companies that are agile enough to offer big banks the immediate ability to experiment and evolve much more quickly and effectively than they could individually, given their size and constraints. Innovative partnerships can offer tremendous capabilities to solve problems and drive effective changes to operations, technology, processes and services."

Exploring and facilitating such partnerships to drive change will require financial institutions to recognize that they are dealing with a whole new category of third-party service providers," Pollari adds. Such initiatives by their nature will, therefore, need to be more experimental and collaborative in order to rapidly solve specific problems and address evolving needs as disruptive changes keep rewriting the rules for doing business.

Banks will need to figure out how to augment their traditional sourcing and procurement practices in ways that are more conducive to working effectively with smaller fintech companies in a more agile, experimental environment where the change is low cost, low risk and quick. It will require a far more collaborative approach than the traditional vendor relationship today's banks are accustomed to."

Top-down strategies are critical

BIG banks that are prepared to engage with fintechs will also need to adopt a very strategic approach that addresses two key perspectives. First, they need to have in place strategic priorities for the changes and new services or models they need to implement. This includes identifying capability gaps that need to be filled or addressed by the bank itself or a fintech relationship. "This will require a top-down strategy on the priorities of the organization and how these are going to drive engagement and interest in fintechs," Pollari says.

Beyond immediate needs and solutions, banks should also be exploring and assessing opportunities that transcend the immediate ecosystem in terms of future capabilities or services.

The right fintech can actually prompt the bank to consider a new opportunity or adjacency they might not have imagined or considered. I encourage banks to dedicate maybe 70 percent of their efforts to addressing current strategic priorities and 30 percent to exploring or pursuing new developments or emerging technology that can really come to fruition quickly for the benefit of their customers or operations.

"The need to remain forward-looking amid the constantly changing landscape will remain critical," Pollari notes, meaning banks need to be committed to the innovation trail. And while some industry players are adapting and moving forward with progressive new engagements, partnerships and initiatives in the face of disruption, many are lagging behind and facing tremendous new risks that include being left behind, or worse, in the future.

A significant number of financial institutions get it and are responding accordingly. But broadly speaking, you could have a third of banks and financial institutions today that are not adequately engaged. And some will struggle in a digital economy where innovative partnerships between Fintechs and large incumbents can deliver rapid and dramatic advances. ***To be continued***