The Platformization of the Banking Industry

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Understand what Banking as a Platform (BaaP) is and how consumer expectations will change under this concept

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Even though banks have advanced over the years regarding the use of digital channels, for a long time these institutions have kept unchanged the vertical essence of their product development and distribution. Therefore, the solutions offered were created in-house and sold through their own channels. However, drastic changes are expected in this sense, since the battlefield is very different from the one where large financial institutions dominated the scene and the barriers of entry for new entrants were very high.

In the late 90s we saw the rise of fintechs, startups that developed specific financial solutions with a great focus on the customer and that used the potential of scale provided by the internet to reach a large audience (having a much leaner structure than banks). These companies expanded as technology costs have been reduced year after year and authorities around the world have created regulations to better accommodate new entities in the financial system. In addition, we started to see the open API movement happening in a voluntary and regulated way (via Open Banking) in different markets, which started to allow different integrations between service providers and banks, subverting the logic of the vertical systems that prevailed until then.

This combination of elements brought about a scenario of greater competition and made the banks begin to rethink part of their business models.

The “as a service” world takes over the financial market

As we move to a less vertical banking reality, we see that some traditional financial institutions and fintechs are making use of approaches in which they offer their capacity and expertise as a service to other companies, in a flexible and on-demand basis.

A model that has been explored by financial institutions is Banking as a service (BaaS), in which they enable the activity of new market entrants through the provision of technology solutions and regulatory interface, being a great shortcut and often the most viable alternative in terms of cost-benefit for those who want to start offering financial services. On the side of those who provide the service, there are institutions that do it as a main activity or as an additional line of business, something that financial institutions and small and medium-sized banks have adopted. It is worth mentioning that a good part of the newest neobanks uses some type of BaaS provider, and this is currently a very heated market on a global level.

On the fintech side, there is also a model similar to the one mentioned above, which in turn is called fintech as a service (FaaS), where these players provide solution modules for third parties ranging from credit to investments, by example, containing all the business intelligence, data analysis capabilities and user experience developed by these companies. The typical customers for this type of service ranges from multi-segment startups to other fintechs. Transferwise, a unicorn in the international remittance business, is a good example of a company that, in addition to working directly with its customers, outsources its technology and expertise to other players interested in adding a new solution to its portfolio. It is worth noting that the agreements to make a FaaS model possible may involve revenue sharing or charging a fee for using the service.

The popularization of BaaS and FaaS shows that these new approaches are thriving and giving new shapes to the financial industry, where different roles can be assumed by banks and fintechs. This new paradigm in the sector ended up bringing yet another interesting thesis that is getting popular worldwide - Banking as a Platform (BaaP).

The Bank as a “Platform”

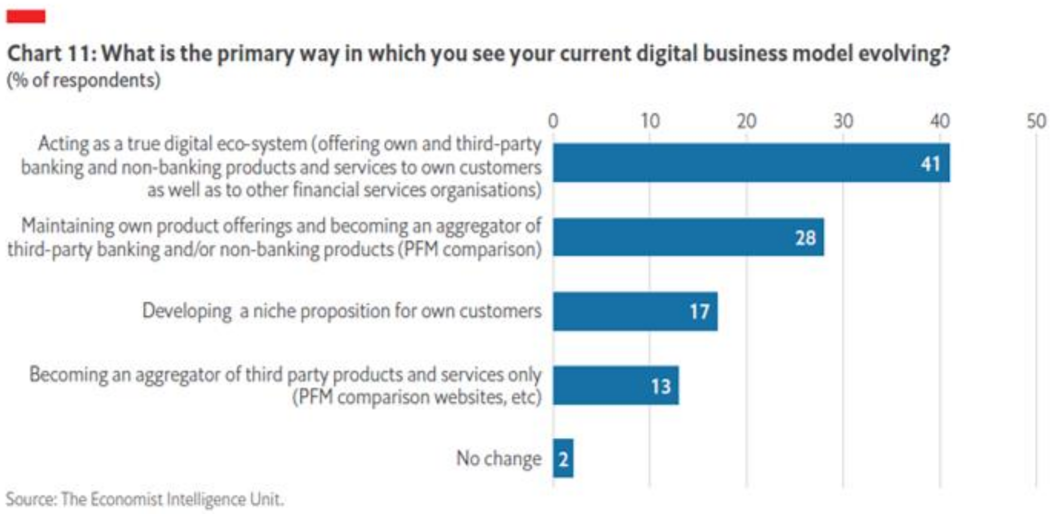
The concept of platforms in the technology world was made possible thanks to APIs and is based on the construction of an integrated business ecosystem, in which multiple agents create solutions that are offered within the same environment. Big tech companies like Amazon and Google formed their empires this way, eventually influencing other segments as well.

Banking as a Platform goes this direction and translates itself into a model in which the bank (or another financial institution) adds digital services from third parties to its portfolio, offering them on its channels. In its offerings, not only are financial products included, but other non-financial solutions that can make the end customer life easier. In platforms like this we can also have the presence of BaaS and FaaS providers, inhabiting this ecosystem.

The British neobank Starling Bank is an example of an institution that positioned itself as a platform that solves its clients' multiple pains. Its business accounts has integrations with third-party solutions ranging from insurance against default of invoices to human resources management and legal advisory tools, among many others.

Adopting a BaaP strategy is much easier said than done, especially when we look at the reality of the big banks that carry the weight of their legacy and have a long way towards restructuring their operations and making the transition to this new context. It is worth noting, however, that a good part of the top players are aware of this need for change.

In 2019 The Economist Intelligence Unit conducted a survey with 405 global financial market executives, who were asked what would be the main way in which they saw the evolution of the retail banking digital business model by the year 2025. Among the 41% of respondents said they believed that banks should develop true digital ecosystems, offering their own and third-party banking and non-banking services to their customers and other organizations. 28% believe that institutions should maintain their own product offerings becoming aggregators of banking and non-banking products from third parties. Finally, 17% believe that they should develop a niche proposal for their own customers, 13% understand that they will become aggregators of third party products and services (acting this way only) and 2% of the respondents believe that there will be no change.



The majority of executives interviewed (69%) have a vision of the future that is in line with the concept of Banking as a Platform, and a large share within this group expects banks to develop complex ecosystems that resemble the reality of superapps such as Wechat, which would need huge doses of technology, collaborative spirit and regulatory encouragement to actually be developed by 2025.

In the future, a broader role for banks

The entry of companies from different sectors (such as telco, technology, retail, among others) in the financial market will also significantly change the perception of customers, who will start perceiving a good part of financial services as commodities. It is at this time that banks that haven't changed their strategy will be in serious danger.

It will be increasingly expected by consumers that the different platforms with which they interact in a daily basis will harmoniously aggregate and facilitate different aspects of their life, through a great understanding of their data and proactive offerings made at the right time. An interesting example comes from the British neobank Revolut, which can understand if you are at a ski resort (via geolocation) and offers daily microinsurance against personal accidents at a cost of 1 Euro per day.

Retail banks will need to have a much broader role than they do today, becoming a kind of digital concierge for individuals, being able to deliver value even in shopping recommendations or suggestions of new restaurants to visit. Looking at busines solutions, on the other hand, they will need to be very close to ERP platforms to anticipate companies' needs and propose operations based on information and projections generated in real time.

In the era of platforms, the operating model is characterized much more by the connection than by the control of the value chain, and this reality finds great synergy with the open finance environment that is soon to be established in Brazil. This attribute deeply affects concepts that are still rooted in incumbents modus operandi. In a report on the topic made by Mckinsey, the message about the risks of inaction in the face of this new scenario is very clear: “Change is rarely comfortable, but as market evolution illustrates, the forces of change are inevitable. Banks are better served getting ahead of and defining the trend rather than waging a futile battle to repel it.”

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About Bruno Diniz

Bruno Diniz is Managing Partner at Spiralem and South America Director at FDATA. Regarded as one of the top fintech influencers in LATAM, Mr Diniz is also a professor, speaker, and author of the bestselling book ‘The Fintech Phenomenon’ (not yet translated).