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Covid-19 crisis: Opportunity for banks to reshape service models and foster digital transformation

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Abstract

The coronavirus situation is causing widespread concern and economic hardship for society, consumers and businesses worldwide. As for entire world, COVD-19 is the most serious challenge to financial institutions in long time. Banks are called upon to manage this new phase with urgency and aptness, to help deflect a worldwide recession. Until recently, majority of banks were focused on empowering both the psychical and digital distribution models. The "new normal" calls for reassessing of priorities and pushes new distribution model where psychical and digital are combined and act as one, with interconnected capabilities. This paper highlights importance of long-term positioning in post covid world, as market forces and customer behavior potentially change coming out of this crisis. In order to manage revenue and customer expectations, new customer-centric and digital-based ecosystem should be established, leveraging on the latest technologies, aiming at increasing remote sales and market penetration. Having that in mind, article aims to shed light on key factors important for retail banking success in this "new future".

Keywords: retail banking, coronavirus crisis response, digital technology, reshaping banking industry, customer experience

JEL Classification: G00, G20, G21

1. Introduction

"The crisis is the greatest blessing for people and nations, because the crisis brings progress… It's in crisis that inventiveness is born, as well as discoveries made and big strategies... Without crisis there are no challenges, without challenges life is a routine, a slow agony. Without crisis there is no merit. In crisis emerges the best of each, because without crisis all winds are only mild breezes." (Albert Einstein 1955)

The COVID-19 pandemic is causing a direct global destructive economic impact that is present in every area of the globe. All parties must now face what has already been obvious to many that such phenomenon is imminently possible and indeed likely. How will this effect costs of capital, pension planning, insurance, the role of governments protecting financial systems, social trust and concomitant transaction costs, and political stability in societies? (Goodell 2020). No one knows the answer, but now is the right time to make long time strategy for the new future that arrived unexpectedly.

Banking activities are non-sanitary essential services, as they are the backbone of businesses, support daily needs of individuals and are the heart and soul of the economy, both at country-level and globally. Banks of course by their nature are vulnerable in times of economic downturns, because of the likelihood of nonperforming loans and the possibility in extreme cases of bank runs (Goodell 2020). As for many other industries, recommendations for social distancing triggered up to 90% bank employees working from home (WFH), as well as physical i.e. branch network closure as a driver for increased usage of online banking. Banks all around the world are working to keep their distribution channels open, despite social distancing advice and supervisory and compliance functions that were never designed for remote work. They're trying to manage revenue and customer expectations, despite near-zero interest rates and growing pressure on consumers. And, they need to keep an eye on strategy and brand issues that will define their future, as market forces and customer behaviors potentially change coming out of this crisis (Source: PwC 2020).

All those facts impose that long-term positioning is very important; it may seem early to imagine post covid world, but it is important to take the long view. Examining what similar researches suggest, we tried to emphasize key factors important for shaping future products, distribution preferences and gain success in retail banking. The paper proceeds as follows: first the author will note major challenges banking organizations are facing due to coronavirus pandemic. Furthermore, the model will be proposed in order to explain the crucial milestones in creating successful banking ecosystem capable to ensure business continuity and support customers and community in proper way, and the main proposition will be summarized in the conclusion.

2. Digital-human interaction is the new normal

Since the coming of the industrial or machine age, society has been continuously impacted by new technologies. The technologies we are exploring today, such as artificial intelligence, gene editing, nanoscale manufacturing, autonomous vehicles, robots, wearables and embedded computing, are radically going to redefine the next age of humanity. Today our progeny measures changes in months, not decades (King 2016). It is difficult to imagine a world without the internet or mobile devices. They have become core elements of our lifestyle and have brought a high degree of disruption to virtually every area of business. Financial services industry is no exception; the digital revolution is transforming the way customers access financial products and services. Although the sector has experienced a degree of change in recent years, the constant penetration of technology-driven applications in nearly every segment of financial services is something new (Global Fintech report 2016).

During the pandemic, there was a general rise in nonperforming loans, decline in the volume of bank transactions, a decline in card payments and a fall in the use of ATM cash machines worldwide. This led to fewer fees collected by banks which negatively affected banks' profit. On the other hand, the lockdowns due to the coronavirus outbreak resulted in higher demand for some sorts of online services such as online shopping (Ozili, Arun 2020). In recent period, banks demonstrated commitment to their customers and wider community, living the values in a real and demonstrable manner. This is likely to become more difficult in coming months. Although banks faced into the covid crisis with stronger balance sheets, they will encounter significant challenges in continuing to support their customers and fulfill expectations from stakeholders (Clarke 2020). COVID-19 is pushing for a severe paradigm shift and reshaping of the banking industry as we know it. The „new normal" pushes a new distribution model.

Until now, banks commercial strategy was focusing on strengthening both the psychical and digital (direct) distribution models. Priorities must be reassessed, COVID-19 calls for the revalidation of the distribution model, where psychical and digital are combined and act as one, with multiple and interconnected capabilities. A new, customer-centric and digital-based ecosystem should be established, leveraging on the latest technologies, aiming at increasing remote sales and market penetration. In this unprecedented fight against COVID-19, digital technologies offer the only opportunity for governments, individuals and businesses to cope with social distancing, ensure business continuity, and prevent service interruptions (World Bank 2020). The value of human touch will be highlighted and will be merged with the efficiency of digital. In other words, where "remote" is the key concept, technology is an enabler and human touch will be precious, value added interaction. Remote offer introduces new way of servicing multichannel customers. With personal banker support, customer will swiftly access support via direct channels while maintaining relationship with the branch.

3. Evolvement of the banking business model under (post) COVID-19 circumstances

There is now an immediate and pressing need for banks to support their retail and commercial customers and the communities at large (Clarke 2020). A crisis often brings out the best in us, and the banking industry is in a unique position to play a vital role in restoring our communities. Whether providing mortgages to growing families or loans to growing businesses, retail banks have a long history of promoting social and economic success. The banking business after COVID-19 shall be intensified with new sources of growth: advisory services, e-commerce, digitalization, e-banking services etc. Online and digitalization will be the way forward. Comprehensive reform and finance sector restructuring programs should be thought of in order to accommodate such changes and speed up the recovery process (Lelissa 2020).

Following existing but still scant literature, we tried to shed lights on elements that are key business drivers under (post) covid circumstances: 1) digital capabilities, 2) customer centricity, 3) new service model, 4) full online services and sales as well as 5) improved communication.

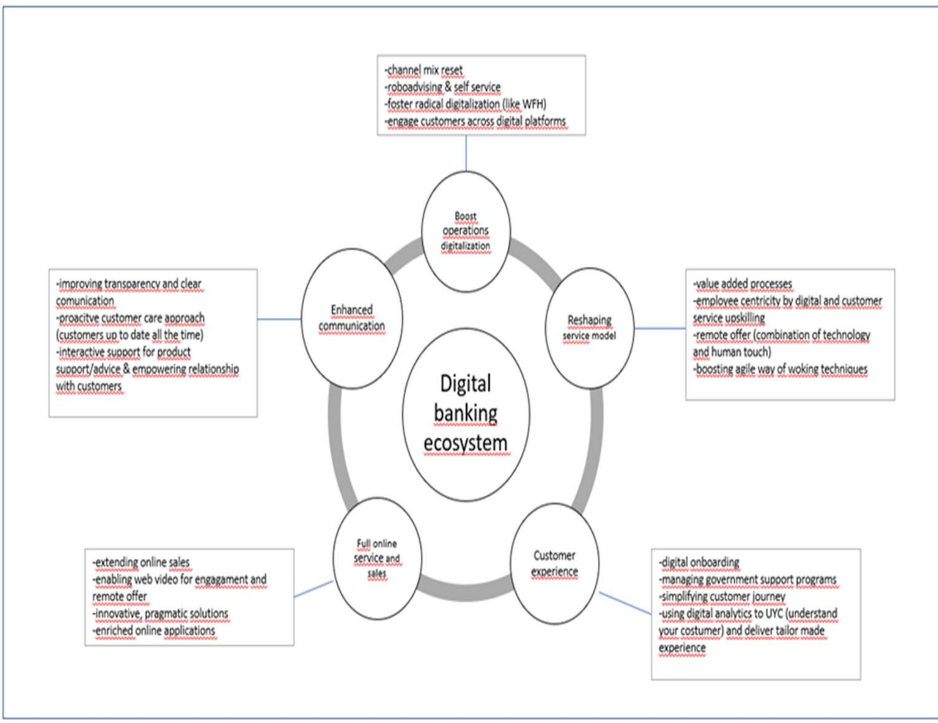

Figure 1. Digital banking ecosystem proposal

The future of banking requires a new perspective on how to deliver services more effectively and efficiently to consumers who have grown accustomed to advanced digital engagement from non-financial institutions. Different business models would generate different network effects and monetization opportunities. The IT platform provider needs to identify the excess value being created by its platform and ways to capture that value in order to effectively monetize the network. Monetization methods can include transaction fees, charging users for enhanced access, charging third party producers for access to a community, and charging a subscription fee. While determining the appropriate monetization strategy, it is important not to create friction that would slow user growth and cause negative network effects (Kansu, Parker 2018).

The "new normal" of banking is quickly moving from branch, bank-centric organizations with legacy technologies and cultures to consumer-centric organizations with more personalized solutions that can be delivered seamlessly. World Banking Report 2020, (Capgemini and Efma 2020) highlights that those firms that can deliver fully digital, platform-based banking will realize significantly lower acquisition costs, an improved efficiency ratio and much lower costs of distribution.

Multichannel environments provide tremendous opportunities for financial service firms and before crisis, majority of banks worked already intensively to leverage on technology and foster digitalization. The digital revolution has changed the demand for financial services and moved the industry to be customer-centered with strong focus on customer experience (Vives 2019). New circumstances are opportunity to accelerate those activities as respond to lasting social changes, including how customers select channel preferences and products for their individual financial needs. Behavioral changes may accelerate the shift of the branch concept away from transactions toward a more complex, high-value operation.

According to Skinner (2014) channels are what banks deploy to reach customers. Customers are looking for service that is relevant to their needs, such as buying a house. Customers what service delivered in the way that is relevant to them and in the way they prefer. So it is not the bank reaching out to customers through channels, but customer reaching out to banks through needs. In that sense, it is more appropriate to talk about omni customers, not omnichannel. The omni customer differs by segment, demographic, perspective, adoption of technology. The bank's challenge is to design the service for every customer so that they get the experience they want. The rapid rise of digital services has driven a change in what consumers expect, in every area of their lives. The approach from Netflix, Amazon, Apple etc. have fueled an "on-demand" and "one-click" mindset that people are no longer willing to overlook when deciding who to give their business to. They now expect every organization to deliver products and services quickly, with a seamless user experience – and financial services are no exception (Markovitch, Willmott 2014).

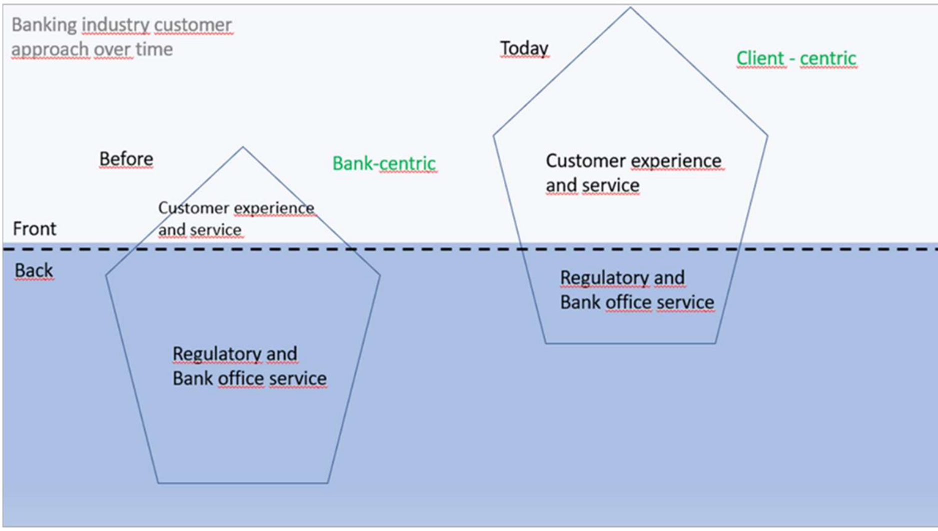

Figure 2. Change in customer approach in banking over time (Source: author)

The changing environment in the banking sector and the massive increase in competition and performance pressure forces banks to find new ways to differentiate from competition in order to be able to compete in the future. Banks are forced into committing to a rigorous customer-centric view in the design of their strategies, service portfolios and enabling process and IT landscape (Dohmen et al. 2009). Customers are increasingly expecting individualized offerings, and leaders will need to use data to fine-tune their customer, product and pricing strategy to deliver on those expectations. Bank online channels and capabilities will play a very important role, efforts will be on dramatically boosting online processes, services and products towards existing clients. Rethinking of commercial strategy and distribution model with strong presence of remote support and offering is required. Branch staff should be involved to provide value-added activities and maintain „trust „of customers despite social distancing, leveraging all aspects of technology to process time-consuming, dispensable and menial tasks.

Putting aside coronavirus situation, over the next decade consumer profile will change dramatically as the Baby Boomer generation ages and Generations X and Y assume more significant roles in the global economy. The latter group, also known as "Millennials" (those born between 1980 and 2000), is bringing radical shifts to client demographics, behaviors and expectations. Dohmen et al. (2009), states that banks have to actively design their appearance in the market, in order to increase sales of financial products in the future. Paper highlights three main strategic considerations that have to be taken into account by banks. First, the scope of services must be orientated on the needs of customers. Second, the design of customer contacts must create functional and emotional value added to the customer. Third, the appearance of a bank has to be adjusted in such a way that (a) trust is created by presence, strengthening brand leverage in all relevant distribution channels, (b) integration of distribution channels and control over channel-wide sales process is ensured and (c) cooperation with service providers who can generate value added for the customer increases the frequency of interaction between the bank and its customer.

The next age of humanity, age of augmented intelligence will bring even a bigger rethink of processes involving dynamic decision-making, pattern recognition and advisory services as machine intelligence optimizes those processes and feedback loops. The so-called Augmented age will bring, among other things, two major disruptions – artificial intelligence and disrupted, embedded experiences (King 2016). Experiences that enable frictionless, contextualized service, products, advice and value creation which, in turn, are monetized base on their effectiveness. Consumers are value-driven — no matter what they're shopping for or how cutting edge the technology is (Meehan 2015). In a world that is permanently augmented by data and information, value, personalization and context will be key for success.

It became clear that just having data was not enough. Firms are being tested to determine if they have a high capability to manage data and utilize the data for the consumer's benefit. According to the Capgemini&Efma research (2020), only 26% of financial institutions had the confidence to classify themselves as "data experts."

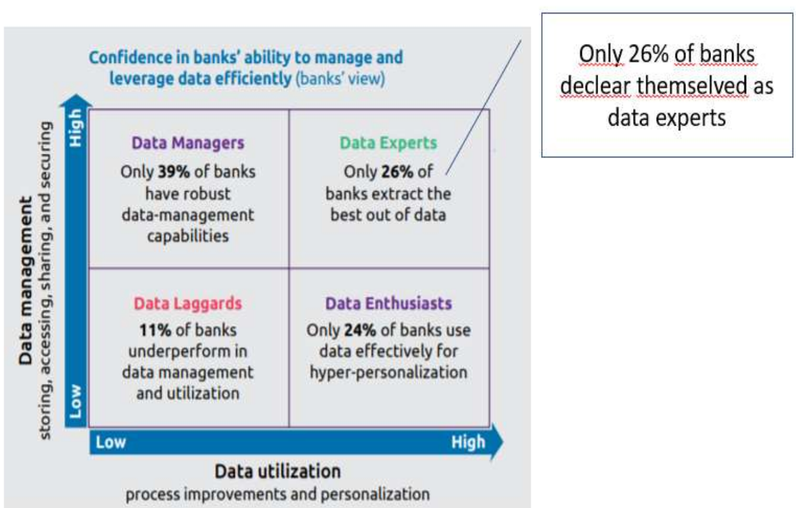

Figure 3. Data utilization and management (source: World Retail Banking Report, Capgemini Financial Services Analysis 2020)

In order to really understand customers, banks should focus strongly on digital analytics and establish tracking strategy using available tools like big data and artificial intelligence. Through a constant comparison by new and existing customer related data, artificial intelligence is a big resource on defining and predicting the customer behavior. Tracking of crucial touch points to gather data about customer behavior is the only way to achieve in-depth knowledge of customer's needs and preferences that, consequently leads to optimization of digital communication and campaign investment. From an economic standpoint, it is also a big opportunity for retail banks to increase automation and reduce the cost of serving customers. This long-term strategy will not only foster business and revenues but will also bring positive effects in terms of cost-to-serve. Furthermore, all data gathered not only support investment allocation, but enhances the chances to fully exploit digital experience based on actual customer needs.

Finally, communication management plans are extremely important in the era of social distancing. Transparent, clear and easy to understand messages, up to date information and interactive real time support can help to increase customer satisfaction, foster good relationship and long-term loyalty.

4. Process design & team skills set for new distribution model

Technology increases accessibility to faster, cheaper and simpler financial services, gaining significant momentum and causing disruption to the traditional value chain. Bank online channels and capabilities will play a very important role but moving quickly isn't always easy. Business decision making is often causing the bottleneck rather than IT development. That's why digitization programs need strong board-level support to align all the stakeholders, while all other decisions should be delegated to the project team. To guarantee the correct support, digital teams within banking company must take immediate action and recalibrate priorities considering the pandemic and the consequences it is having and will have. With a government policy that caused people work from home, people will get used to working with virtual teams and the society will be more understanding of technology. Companies can also learn from current conditions to be more dynamic in the future. In addition, manual origin processes will be replaced by digital processes because with this outbreak, all processes are carried out digitally (Vashti 2020).

Fast-changing and uncertain business environment of the new economy imposed by digital era, address new organizational capabilities and competencies which imply that banks need to redefine traditional approaches of doing business, to adapt to changes faster, more efficiently and effectively (Tornjanski et al. 2015). Complete organizational re-engineering is needed, as well as rethinking of commercial strategy and distribution model with strong collaboration among employees with business, tech and service design skills, able to adapt quickly to the new conditions. In order to establish entire new processes and reshape service model, wide variety of perspectives, skills and tools is crucial to understand best solutions and design the quick win processes to easily support customers. To meet these high customer expectations, companies must accelerate the digitization of their business processes. But they should go beyond simply automating an existing process. They must reinvent the entire business process, including cutting the number of steps required, reducing the number of documents, developing automated decision making, and dealing with regulatory and fraud issues. Operating models, skills, organizational structures, and roles need to be redesigned to match the reinvented processes. Data models should be adjusted and rebuilt to enable better decision making, performance tracking, and customer insights. Digitization often requires that old wisdom be combined with new skills, for example, by training a merchandising manager to program a pricing algorithm. New roles, such as data scientist and user-experience designer, may be needed (Markovitch, Willmott 2014).

To reimagine banking in a post-pandemic world, there needs to be a focus on both disruptive technologies and innovation, as opposed to simply moving forward in small steps. The winners in the future will be defined by those organizations that can leverage digital technologies to deliver a customer experience that goes beyond the ordinary. In most cases, this will require a collaboration with fintech and potentially bigtech partners (Morous 2020). Important is to create center of excellence with skilled employees that can be called upon to digitalize processes quickly. Often companies must search talents externally to address the need for new skill sets and roles. It is crucial that managers initiate a clear strategy for online channel development. Marketing managers should learn from earlier investments initiatives, where a lack of articulated strategy, well-grounded ambitions, and development of dynamic capabilities creates early disappointment (Maklan et al., 2011). Managers given the role to lead the transformation should be carefully selected, with good references and ready to commit for long-term. Team they lead should be skilled in modular way so they can be reused across processes, maximizing economy of scale. When digitalizing selected areas, end-to-end process should be tackled to deliver truly seamless and frictionless processes. The definition of a strategic path for establishing clever banking goes through a combined model of business, organization and IT strategies, able to identify solutions and state-of-art models which can create a sustainable competitive advantage on the market.

5. Conclusion

A crisis brings disturbance, fears and uncertainty but often also gets out the best in us. The need to move to a more digital banking model has been talked about long tie, but coronavirus pandemic has made the need for reduced operational costs and improved digital experiences more important than ever. The banking industry is in a unique position to play a vital role in restoring our communities, by accelerating digitalization and reshaping service model with using resources already present within organization – technology and humans. Complete rethinking and re-engineering of the organization and distribution model should rely on cutting edge technology (artificial intelligence, big data etc.) combined with human touch to optimize cost-to-serve, gain revenues, provide support to community and deliver outstanding customer experience. Companies that digitize processes can improve their bottom lines and delight customers, despite social distancing circumstances. Delivering great customer experiences now can help businesses drive loyalty and revenue in the long run.

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