# Future of Retail Banking

## 5-Year Vision

By Philip Farah, Cisco IBSG Financial Services Practice

As we look into the future, away from the ebb and flow of daily market fluctuations, clear trends on many fronts will no doubt alter the future of retail banking:

- **We're aging** (with some exceptions, including India and my fellow tai chi practitioners), with over-60s becoming the fastest-growing age segment (note that I'm not addressing the idea of ultra-longevity as we become capable of growing new organs or modifying our DNA programming).
  - This means fewer loans to buy homes and cars, or to get kids through college, and possibly more demand for the financing of health needs. It also means new interaction requirements (for example, the ability to connect to your banker over video from a residence or retirement home instead of having to physically visit the branch). Equally important is the need for banks to offer new products and services that help customers deal with insufficient retirement savings and growing medical costs magnified by increasing longevity. Banks also have the opportunity to help seniors stay employed longer by creating new job opportunities for this segment above and beyond the occasional retail clerk position. Will banks partner with employment sites to create a home-based, tech-enabled job market for seniors that competes with the economic advantages of offshoring?
- **Our governments are financially broke!** This is especially true in developed economies, with more than $60 trillion in unfunded medical and retirement liabilities for the U.S. government alone.
  - With governments deleveraging—often in parallel with a similar trend in the private sector—we're witnessing short-term downward pressure on GDP growth. Looking forward, this will result in a slowdown in government spending on infrastructure and services such as education and medical (we've already discussed the consequences of a reduction in pension disbursements and medical coverage), as well as increased taxes/regulation and greater urgency to enable job creation as a way to enlarge the taxable pie. The effect of increased taxes on individuals is still unclear—for instance, how will a 15 percent to 30 percent increase in marginal tax rates on investments affect the behavior of individual investors? Meanwhile,



 

regulation is here to stay, if only as a preventative measure against future bubbles triggered by FSIs left unchecked. In the United States, changes in regulation are already impacting the profitability of investment banks (proprietary trading bans) and retail banks (interchange fee limits for debit card transactions), forcing banks to rethink their fee structures and accelerate innovation programs targeting new forms of revenues (for instance, new value propositions around merchant-funded offers delivered to mobile devices).

- **We need jobs!** The United States needs them to stabilize its housing market; China needs them to transition to a consumer economy. Forget about the pursuit of happiness and self-realization—according to a global Gallup survey, what global citizens want above all is a decent job. In numbers, we need “only” 1.8 billion jobs for the unemployed out of a global pool of 3 billion.
  - Overwhelmingly, these jobs tend to be created by small and medium-sized businesses (SMBs). This means that we can expect significant economic and government focus to gravitate, in the future, toward the development of the SMB sector. This will create growth opportunities for banks, both in their traditional offerings (for example, issuing business loans) as well as in new value propositions (for example, offering SMB customers cloud-based business apps to help them get their operations off the ground cost-effectively, or even advertising SMB customers’ products in the branches or on a bank-supplied mobile app). Additionally, banks could use consumers’ payment and location information to help new businesses decide which location to choose. One of the major themes of tomorrow’s retail banking is indeed the opportunity to expand the value proposition to become an enabler of life and business goals.
  - The nature of tomorrow’s jobs is also evolving. As new industries emerge, the need for training/certification and a workforce that can easily move around industries and geographies will continue to increase, creating opportunities for banks to finance all of this or to enable person-to-person lending where needed.
  - In addition, as more of our lives and assets migrate to the digital realm (thanks to mobility, social media, and pervasive sensors, with clouds/big data in the background), so will economic value creation. It means that the portion of GDP generated in the virtual world will continue to increase (for example, Internet versus traditional media). It also means the likely emergence of new revenue and compensation models rewarding one’s ability to sense and influence other people’s intentions before they get translated into action (social influence). Banks will have the opportunity to use digital footprints to proactively address their customers’ needs and issues. Other opportunities include the ability to help SMBs expand their business in the social media domain or to offer back-office support for seamless value exchange rewarding one’s social media influence/interactions.
- **Growth will continue to be bimodal.** With the growth rates of developed economies in the low single digits while developing countries exhibit high-single-digit/low-double-digit growth, China’s GDP could surpass that of the United States over the long term. Most important, the emergence of a massive middle class within the developing world will balance the adverse impact of reduced spending due the aging population. In developed countries, the best predictor of spending is the size of the age cohorts,

whereas in developing economies, it's the size of the employed population. As a result, major opportunities for retail banking will migrate to those countries with fast GDP growth and an emerging middle class.

- **Technology is radically changing the way we live and work.** We now receive offers based our location and can compare prices in retail stores using our mobile phones; Facebook and Google know us better than our shrink; Apple stores our pictures in its iCloud; video is part of our business and private communications; and sensors are penetrating our cars, homes, and hearts.
  - The implication is that *Omnichannel, not multichannel, will redefine the way customers interact with their banks***.** In other words, the ability to connect with customers in new and more intimate ways— for example, serving them personalized offers on their mobile phones or home video-conferencing system based on their location and social media interactions—will trump previous models that focused on migrating customers to cheaper channels or ensuring consistent look and feel across channel.

## Pillars of a New Value Proposition

The emergence of the Omnichannel era, combined with changes in demand as a result of global demographic and economic trends, will lead to major transformations in the retail banking value proposition along the following two dimensions:

- **Contextual banking** will emerge as the winning banking model in the future. It's a world of seamless banking where financial offers come to you at the place and time of need—and where you will not be asked to go out of your way to financially enable your life goals.
- **Banks as life enablers:** As we move into a world of contextual/embedded banking delivered across a variety of channels, banks will have the opportunity to start cost-effectively orchestrating some of our key life/business goals, such as helping find a house for someone starting a new business, and providing key business services above and beyond mortgages or small-business loans.

## Implications for Distribution, Marketing, and Business Models

- **New branch distribution model:** Forget about the space-age branch of the future, including concept branches that make for better YouTube videos than economics. Next-generation branches will need to add value that cannot be replaced by a mobile/digital channel. They will need to build on the relationship, community, and advice pillars that justify the visit while maximizing customer convenience and efficiency for the bank. So, expect your banker to be able to pull other experts into the conversation using video conferencing, or tellers to be able to manage multiple queues at an airport check-in counter. As an SMB, expect your branch to offer you the ability to connect with your own customers using the bank's video-conferencing capability, or to run product offers on their touch screens. Also expect new formats of banking pods/stations (possibly manned remotely over video) to start being tested in malls and maybe car dealerships.
- **Mobile banking and mobile payments/commerce** will emerge as dominant channels for financial interactions beyond the traditional checking of balance, transfer

of funds, or paying bills and friends through your phone. Mobility is already transforming e-commerce by enabling comparison shopping in stores and delivery of personalized offers based on shoppers' location and preferences. And soon, near field communication (NFC) proximity payments will close the loop between advertising and execution. More broadly, the rise of mobile devices as a platform of choice will finally enable banking to become truly contextual and integrated in people's lives. For additional information, check the blog post titled "On the Future of Humanity…And Payments!" at http://blogs.cisco.com/financialservices/on-the-future-of-humanity%e2%80%a6-and-payments/

- **Social media banking:** New capabilities are allowing customers to access banking services through Facebook; enabling person-to-person lending schemes, with the bank acting as custodian; and permitting banks to take your social networking potential into account when evaluating your credit.
- **Video banking:** Video communications—whether in the form of Cisco® WebEx® web conferences, immersive/high-definition video conferencing (such as Cisco TelePresence®), YouTube, or mobile-based video—is now pervasive. Expect video sessions with your financial adviser from your home/office, as well as video-based mortgage offers sent to your mobile device when you point it to a house for sale.
- **Prescient marketing:** In tomorrow's Intention Economy, understanding people's intentions and needs before they act on them will be critical and achievable. By providing you with the right incentives, banks could tap your social network to learn about your upcoming wedding weeks before it happens, determine you're considering buying a house by analyzing your Google searches, or realize you've relocated to a different state based on your mobile location.
- **Banking in the era of the "Internet of Things":** Today, sensors are invading home structures, home automation systems, trees, livestock, cars, and even humans (pacemakers, for instance, can communicate wirelessly with the Internet and pills can send a wireless signal when they have dissolved in one's stomach). Would you like to be able to enter into an agreement with your bank that'll automatically issue a HELOC to cover your roof replacement costs and issue a work order to a crew of affiliated repairmen when the sensors indicate your roof has reached its end-of-life.
- **Banking and the cloud:** For some, the cloud is a digital hub that can enable alternative payment systems, trading exchanges, or massive info exchange. For others, it is a marketplace for software developers (think the Apple App Store or Google Apps Marketplace) in search of new opportunities. For subscribers (enterprises and SMBs alike), it can simply represent a way to source applications, storage, and compute cost effectively. Banks are already looking into ways to address all three aspects to increase internal efficiency and relevance to clients.
- **Digital identity management:** As we spend more time in digital (or hybrid) environments, banks can provide authentication and identity management capabilities (for example, retinal scanning in fast-track lanes at airports, or confirming you're a legitimate contributor when posting a comment on the web). This would enable banks to ensure privileged access to end-customers' info and possibly create new sources of revenue. This sure beats the 22-cent deposits to your bank account used by various FS players to confirm your identity!

- **Gamification** will gradually replace other forms of training, modeling/simulation, and information dissemination, making financial management more accessible, fun, and in line with approaches of younger generations. Developing such an infrastructure is a complex project. Banks can minimize risks and costs associated with such a venture by selecting infrastructure providers that offer a suite of integrated products/channels vs. trying to take on the task of integrating disparate "best of breed" platforms. Over time, the need for readily available integration will favor the migration of some of the features to an As-a-Service model.

## The Way Forward

So how can banks prepare for these upcoming realities?

- **Invest in a future-proof, Omnichannel-ready infrastructure** that accommodates new interaction channels and is integrated into existing core banking apps.
- **Strengthen your Innovation DNA:** Set up an innovation acquisition and incubation structure with an open innovation mind-set that involves other innovative participants and startups from various industries. The operating model has to enable new ideas to be developed away from the core business to avoid de-prioritization risks, yet with a clear path for integration into the core business when ready.
- **Actively pursue employee and operational productivity initiatives** to free up the funds needed for the customer-facing transformation journey. These include internal collaboration and data center virtualization schemes, paperless/thin desktops, and more.
- **Restructure your organization** around customers and channels rather than existing product-centric models.
- **Cisco can help** your organization in transitioning to an Omnichannel environment. We offer:
  - A dynamic perspective on the role of technology in enabling future industry competitive dynamics based on long-term trends and innovation in adjacent industries (e.g., retail, telecom) as well as FinTech startups
  - A proven approach to ensure investment in enabling capabilities translates into value capture from new value propositions
  - A world-class, integrated infrastructure platform that supports video, contact centers, data storage, and analytics on multiple devices anytime, anywhere... and is proven to scale across the enterprise

For more information, contact Philip Farah at phfarah@cisco.com. For related blog posts on the future of the retail banking industry, check "2011—A Year of Renewal for the Financial Services Industry" at http://blogs.cisco.com/financialservices/2011-a-year-of-renewal-for-the-financial-services-industry/

## More Information

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