HOW CAN BANKS BALANCE DIGITAL TRANSFORMATION WITH IT COSTS?

WHITE PAPER

Digital transformation can mean huge investment – according to research company Ovum, the top 1,000 retail banks spent $124 billion on IT in 2018 alone. While traditional banks are right to continually improve their IT, how can they do it in a way that doesn't overstretch their budget?

INVESTING TO REMAIN COMPETITIVE

Growing competition in banking is understandably putting pressure on traditional players to transform. But why are they spending so much? Costs associated with continuing compliance with rapidly and regularly evolving regulation is of course one driver. Another major reason is that banks recognise the need to remain on the cutting edge of technology in order to remain competitive. In fact, a 2017 study by Zeb found that an average top 50 bank in Europe spends 10 – 20 per cent of the overall banking operating expenditures on IT infrastructure for fear of losing their competitiveness or becoming less efficient.

It is unsurprising that traditional banks are willing to invest such large sums in their IT systems. Consumer habits and expectations have evolved drastically over the past five to ten years, creating a market in which challenger banks such as Monzo and Starling, who have developed highly customer-centric and mobile-friendly models of banking, can thrive.

And with the rapid development of new technologies making it possible for legacy banks to offer app-based solutions, just like their fintech rivals, but also a true omnichannel experience, financial institutions are becoming more inclined to invest with a view to offering customers improved service and experience.

What are banks spending their money on when it comes to IT services? There are expenses to account for in every level of a bank's ecosystem from licencing and implementation to operations and maintenance, as well as fund mobilisation management. These can form a large part of total IT expenditure. The costs of modernising outdated machinery and solutions often also make up a significant portion of spend, as can ongoing technology maintenance, which can make up over half of banking IT budgets according to CSC and Finextra. The result is usually the combination of all these overheads quickly adding up and eating into the bank's profit margins.

CONSIDERING IT AS PART OF THE BIGGER PICTURE

Innovation continues to drive technological advances in the financial sector, and of course, banks should explore innovative new solutions, but they should also keep an eye on costs and ensure every purchase is worthwhile when investing in IT systems. The universal trend of banks investing in the latest hardware and software is unlikely to slow down any time soon – there is no end in sight.

The road to digitisation is often not just an IT decision but part of a bigger picture – the Corporate strategy. By allowing different departments to work together and identify the need for investment, IT expenditure can be more accurately determined. When IT and business strategies are well integrated, IT efficiencies and effectiveness can be better optimised. One way to reduce IT costs in relation to digitisation and innovation is, for example, the greenfield approach. According to this discipline, financial institutions are able to develop new services from scratch without tapping into pre-existing, legacy infrastructures attached to business processes, while also saving valuable resources. Fintechs, such as the aforementioned Monzo and Starling, have enjoyed an advantage by taking exactly this approach and providing mobile-only services. They have avoided the need to contend with the complex architecture of legacy IT systems faced by high street banks.

BEING OPEN TO OUTSOURCING

Outsourcing routine tasks that do not require the time and expertise of employees also offers up the opportunity to save money. For example, external organisations looking after data centre operations, which will ultimately improve company workflow. However, it’s still crucial that banks keep an eye on the costs of hiring partner organisations to ensure they don’t hike up.

Likewise, a company’s infrastructure can be migrated from on-premise to the cloud. By outsourcing services to the cloud, financial institutions have additional resources to develop their core business and focus on incremental improvements to their systems. Part of this can be the optimisation of mainframe applications – applications that are essential to the business can be transformed into more modern and cost-effective environments without affecting stability, security, or performance.

CHALLENGING THE STATUS QUO

You may need to streamline your branch network but banks should always be thinking creatively about how they can serve your customers in other ways, for example by creating 'banking hubs'. This model is already established here in the UK; Lloyds Banking Group, Royal Bank of Scotland, and Barclays recently opened their first banking business hub in Birmingham. These offer small and medium-sized businesses more flexibility in running their day-to-day operations, such as managing large bank transactions from more than one provider, at a one-stop shop.

Retail banks could economise in the same way, by sharing branch and location costs with white label bank branches. This would also provide a seamless customer experience for those from a variety of bank providers, as it means that they can visit a local branch and take advantage of the whole range of services provided by their bank, for which they would normally be required to travel to the nearest "legacy" branch. 'White label' ATMs, frequently owned and operated by non-banking establishments, can also offer an alternative for banks looking to lower costs.

Ultimately digitisation isn't expensive from the bottom up. With the right approach banks can continue to develop innovations and optimise their IT infrastructure, whilst simultaneously keeping operating expenditure low to maximise profitability.

Auriga
Building 3, 566 Chiswick High Road
London W4 5YA - United Kingdom
www.aurigaspa.com
london@aurigaspa.com