

GLOBAL RETAIL BANKING 2019

The Race for Relevance and Scale

October 2019

By Thorsten Brackert, Chaojung Chen, Jorge Colado, Laurent Desmangles,
Muriel Dupas, Pierre Roussel, Holger Sachse, Sam Stewart, and Monica Wegner

Boston Consulting Group partners with leaders in business and society to tackle their most important challenges and capture their greatest opportunities. BCG was the pioneer in business strategy when it was founded in 1963. Today, we help clients with total transformation—inspiring complex change, enabling organizations to grow, building competitive advantage, and driving bottom-line impact.

To succeed, organizations must blend digital and human capabilities. Our diverse, global teams bring deep industry and functional expertise and a range of perspectives to spark change. BCG delivers solutions through leading-edge management consulting along with technology and design, corporate and digital ventures—and business purpose. We work in a uniquely collaborative model across the firm and throughout all levels of the client organization, generating results that allow our clients to thrive.

Contents

02 | The Future Is
Stacked

20 | The Options for
Incumbents

06 | Where Retail
Banking Is
Going

24 | Build New
Capabilities
Now

14 | The New
Battleground:
Relevance and
Scale

27 | Conclusion

The Future Is Stacked

The future of retail banking starts with the consumer. Behaviors are shifting, sometimes dramatically, led by consumers who want seamless digital banking solutions embedded in their daily lives. These changes are quickly spreading across all segments and age groups. More people are demanding simple, trustworthy products and services from financial institutions—or other companies offering similar services—that put them first. The combination of these expectations and technology-enabled solutions is fundamentally challenging the advantages of traditional banks (such as branch networks, trust, sticky customer bases, and proprietary data) and opening opportunities for newcomers.

One result, as we explored in 2016, is an almost gravitational pull away from vertical integration and toward a platform-based or “stacked” industry structure. Battle lines are being redrawn at multiple layers of the stack, and the race for relevance and scale among banks and between banks and new entrants has begun.

Technology is fundamentally changing the structure of B2C industries, from competition between vertically integrated companies to horizontal competition in each layer of what we call industry stacks.

For incumbent banks, the shift to a stacked structure will undermine the advantages of integrated value chains as differing economies of scale by layer of the banking stack drive the emergence of new business models. For example, at the top of the stack, companies that offer better (or more attractive) customer interface options can provide consumers with a broad variety of financial and other services through ecosystems, without having to develop their own banking products and infrastructure. At the infrastructure end of the stack, banking-as-a-service platforms can give new entrants regulated account-keeping capabilities at the lowest possible cost, enabling these players to attack fast. Companies that develop specialist products and services in a single vertical industry segment, such as mortgages or payments, compete with a focused set of products and act as a product factory for new distributors. At each layer of the stack, technology enables the modularization of services and challenges the integrated universal-banking model.

The new battleground requires new capabilities. These include the ability to continually create relevant solutions for customers, extract substantially greater value from data and analytics (the basis for personalization in banking), reach beyond traditional geographic borders, and integrate with partners and ecosystems—all while continuing to comply with tough requirements from customers and

regulators for institutional security and good conduct. Banks that don't move quickly risk losing relevance with consumers, especially younger ones, who are the primary drivers of future growth and market share.

This transition is occurring at an ever-increasing speed, which means that retail banks must rethink their positioning and business models. We see four new or modified models that are viable in a stacked world and suited for incumbents: digitized full-service banks, open banks, ecosystems, and product engines. (Of course, traditional banks can also consider entirely new, purely digital growth models in parallel with changes to the core business.)

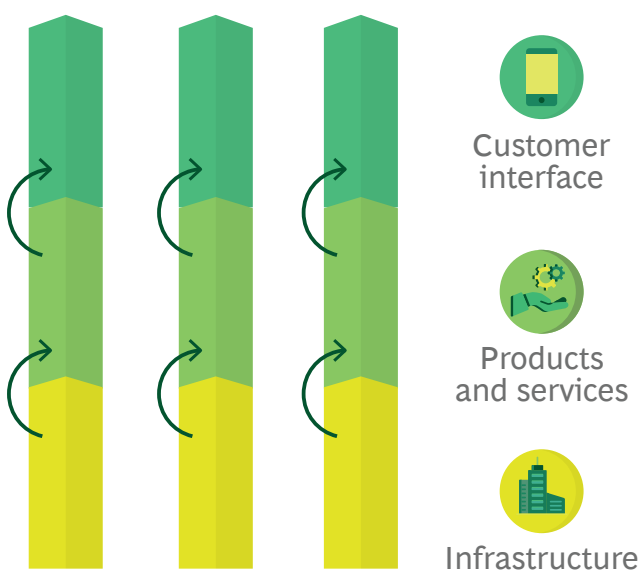
The pace and shape of disruption will differ by market. In some, it's likely that incumbents will lead banking in the future. In others, incumbents will consolidate as challengers gain share. In others still, ecosystems will win big by taking over customer interfaces and relationships, and incumbent banks will morph into utilities.

Precisely how banks should respond depends on where they stand today. Some incumbents must first build a viable digital foundation. More-advanced institutions can select their model and strategy and invest decisively in the capabilities they'll need to build relevance and scale going forward.

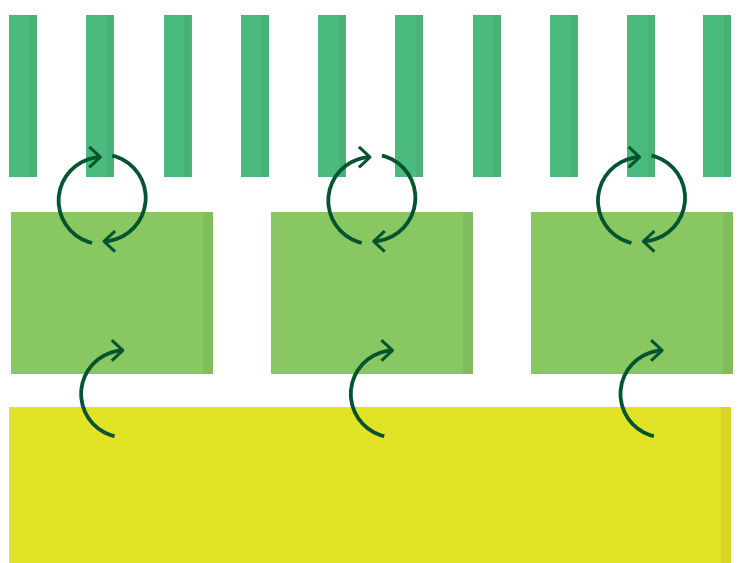
We explore all these changes and their ramifications in this report.

From Value Chains to Industry Stacks

The 1990s: value chains



The future: stacks...

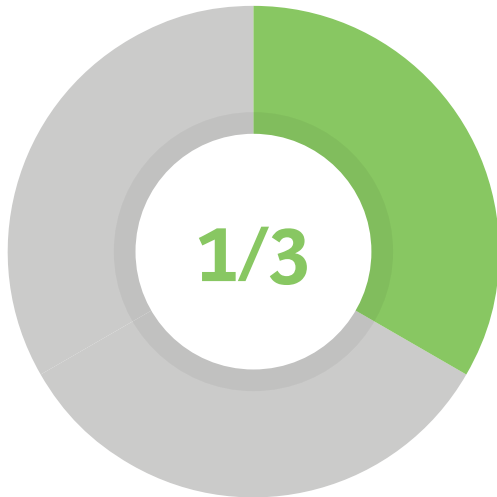


Source: "Will Industry Stacks Be the New Blueprint for Banking?" BCG, June 2016.



**The transition to a
stacked industry is
occurring at an ever-
increasing speed**

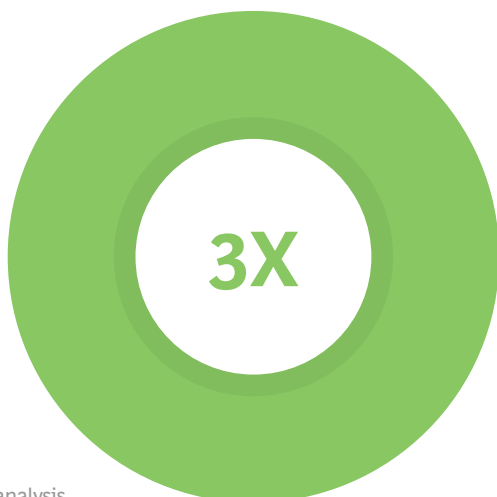
The Future Is Happening Today: Three Facts



One-third of personal loans originated by fintech lenders in the US



One million customers reached 3.5 times faster by neobank Monzo (UK) than a branch-based challenger bank



Among people 25 or younger in China, three times more users for WeChat than credit card customers for the five top banks combined

Source: BCG analysis.



Where Retail Banking Is Going

In developed economies, bankers can no longer rely on market growth. At the same time, consumer behaviors and expectations are undergoing some of their most radical changes. Technology puts more information and choice in consumers' hands than ever before.

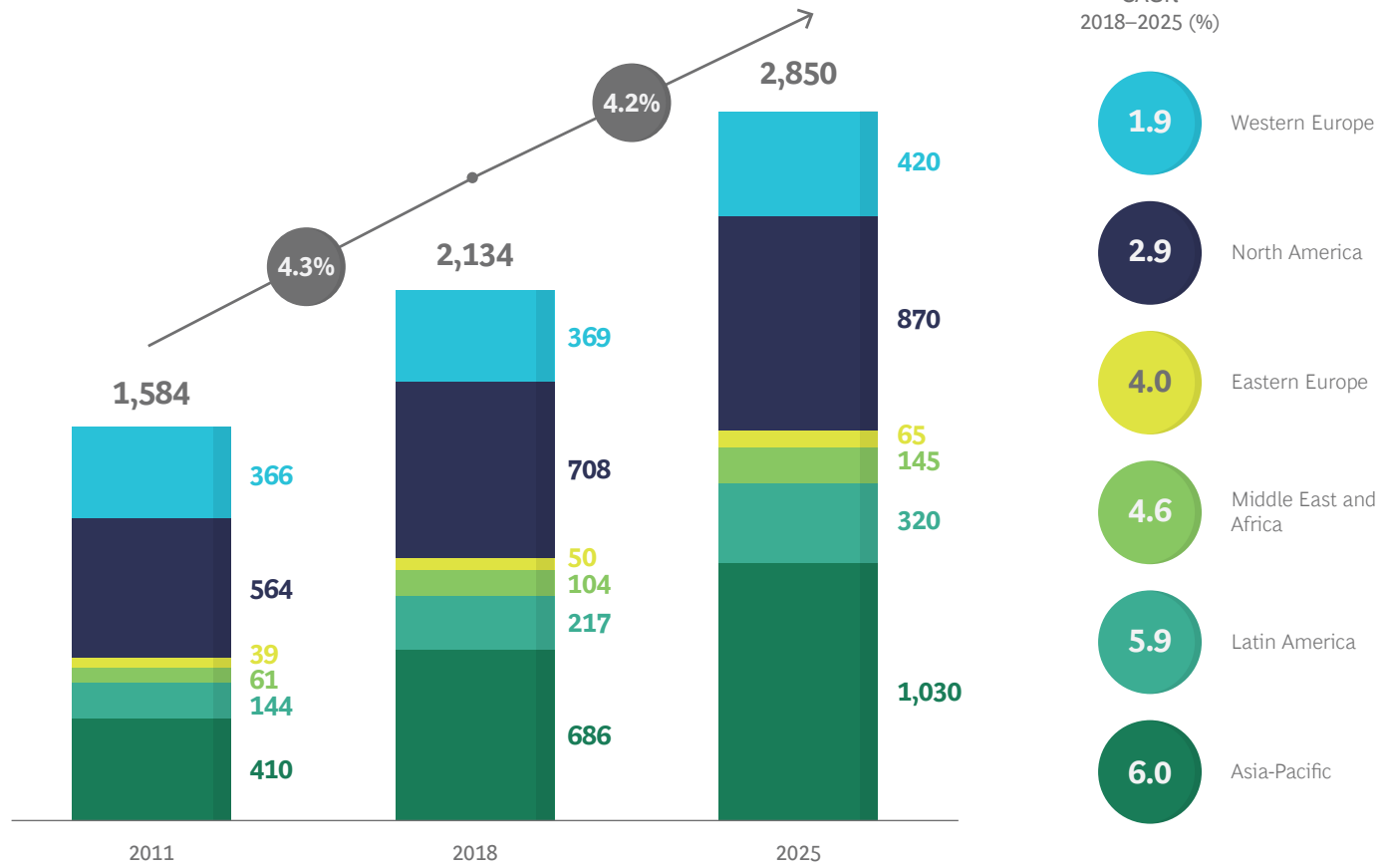
While there is a clear trend toward more digital engagement, human interactions still matter. For banks and customers alike, this means that branches remain an important channel in some geographic areas. At the same time, other innovative means of interaction (video or web chat, for example) are being explored. For some consumers, human interaction is an essential part of the customer experience and banking relationship. Financial decisions can be complex, high value, and emotionally important. People therefore value advice from knowledgeable experts that helps them make the right choices and fill in gaps in the services they are seeking.

For banks, a branch presence is an important billboard; it builds trust, credibility, and brand reputation. Branches demonstrate community engagement. The challenge is to continue to build trust and credibility in a digital world while finding new ways to interact virtually with customers.

Global Market Growth

Emerging markets will be the growth leaders, but mature markets also offer opportunities.

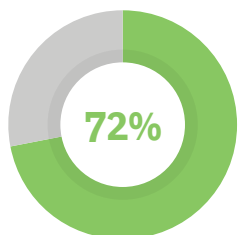
Retail banking revenues (US\$billions)



Source: BCG Banking Pools.

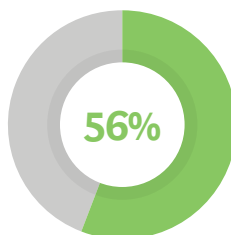
Consumers have new values and priorities.

Online engagement



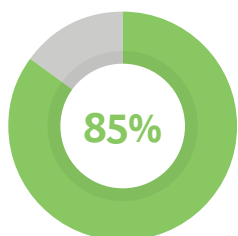
Millennials who agree to the statement: “I enjoy shopping the most when I can do everything by myself online”

Brand relevance



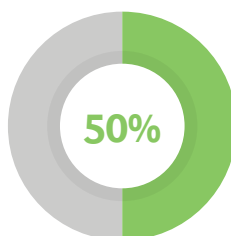
People who want brands that say something about “who I am, my values, and where I fit in”

Data and trust



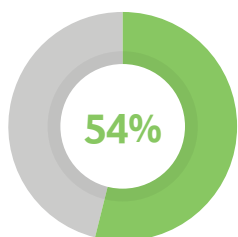
18- to 24-year-olds who would trust third parties to aggregate their financial data

Voice



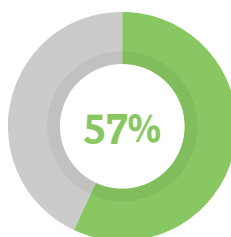
Searches that will be done by voice in 2020

Data for value



Customers who would provide their personal data if they get relevant offerings and operations in return

Ownership



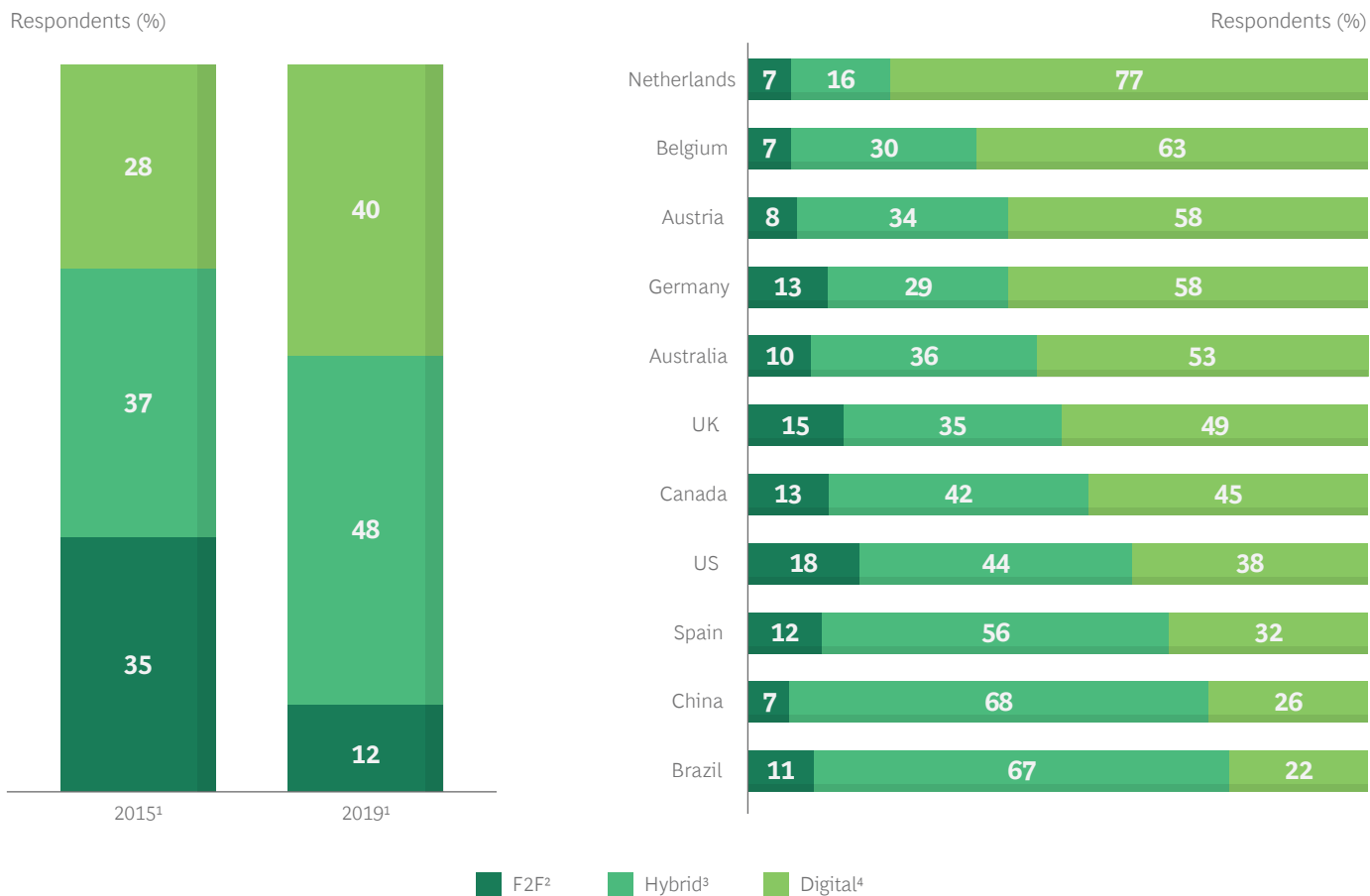
Sharing-service users in the US who might give up ownership altogether

Sources: Research; BCG analysis.

The share of digital and hybrid customers continues to increase.

The share of digital and hybrid customers has increased significantly since 2015. Face-to-face (F2F) customers are now the exception.

There are big differences among countries with respect to hybrid versus digital customers. F2F is the least used channel in all countries.



Source: BCG Retail Banking Excellence Benchmark (REBEX) survey 2015 and 2019.

¹Average across all countries included in the consumer surveys in 2015 and 2019.

²F2F customers are those who do most of their banking through branches and seldom carry out digital transactions (once a year or less).

³Hybrid customers are those who conduct online transactions and visit branches frequently (at least every two to three months).

⁴Digital customers are those who carry out digital transactions frequently (at least every two to three months) and seldom visit branches (once a year or less).

And these customers are doing things differently, for multiple reasons that are relevant to banks.

Human mindset

Financial empowerment

Customers want to satisfy underlying needs, such as feeling secure and making the right decisions. They expect the companies they do business with to put them first and to recognize their individual circumstances. They do not expect to be categorized and put into “segments” along with millions of others. They want to stay in control and make informed decisions. They pay for what they value.

Multigenerational differences

Younger consumers have different needs and expectations than baby boomers. They expect to interact with banks on their own terms and in their own ways. The “one size fits all” approach to banking products, services, and interactions will need to evolve.

Security

Trust

Consumers today put greater emphasis on companies’ purpose and values. They expect that their bank will keep their information safe and will act for the customer’s benefit. They want their money to be safe, an advantage for large and established players.

Control of data

Customers want to own their digital identities and manage the use and monetization of their data. They are willing to let companies use their data—if they receive clear value in return.

Technology-driven behavior

Next-generation interfaces

Mobile devices have already reshaped banking, but they are only the beginning. Voice recognition, virtual and augmented reality, and artificial intelligence are creating new customer interfaces and business platforms. They are also key enablers of new services and will intensify competition between product and service providers.

Sharing economy

Younger consumers are fueling the sharing economy with evolving views of buying and owning (or not), which have big implications for traditional bank products such as auto loans and will drive the development of innovative solutions.

Relationship to banks

Build your own bank

Open banking, in particular access to products and services built by third-party developers, allows customers to build their own bank by combining products from different providers on a single platform. This threatens the primary banking relationships that have been at the heart of incumbents’ strategy and forces banks to become part of relevant ecosystems.

Invisible bank

Customers want financial solutions woven into their daily life. They see no reason that these solutions cannot be integrated with answers to adjacent or underlying needs, often via ecosystems.

Traditional banks' competitive advantages will erode over time

Paradigm Shift

It all adds up to a paradigm shift for incumbents. Traditional competitive advantages, including large bases of sticky customers, will come under significant pressure. Physical networks, captive pools of data, and scale within markets will give way to digital networks that undermine physical networks' role as a barrier to entry. Competitors with access to new sources of data—including previously proprietary bank data—and scale both within and increasingly across borders will take advantage of network effects from growing numbers of customers or users.

Data access allows new competition

Data Banks used to have a data monopoly. Today, even as more banks are making use of the troves of behavioral and transaction data they have access to, this data is also accessible to third parties, eroding banks' advantage. In addition, as customers leave data footprints in more places, new sources of data are emerging in unprecedented volume and can be used by all kinds of players for financial-industry needs, such as credit decision services. Tech giants are particularly adept at capturing and using data from new sources.

Physical networks become a less significant barrier to entry

Networks Banks used to compete on the basis of branch networks and human advisors. As customers increase their use of digital channels—and some engage only digitally with their financial-services providers—the value of these networks erodes. New platforms (such as e-commerce sites and social networks) and digital interfaces (such as phones and voice assistants) can provide equal, or unequal, access to multiple financial-services providers. The goal of these new players is to provide convenience and choice to consumers and thus build the number of users and the amount of data on their platforms. As parts of the customer base still value and use them, branches will be important for incumbents. But their role is going to change fundamentally, with a new focus on brand presence and high-value interactions rather than service.

Network effects challenge current sources of scale

Scale The need to keep up with the pace of change—in customer demands and behaviors, technology, and regulation—is continuously increasing. The ability to build high-quality capabilities at speed requires scale in terms of the number of customers. A new force is at play as well: network effects cause the value of a platform to increase for all customers as the user base grows. Some players might be able to apply capabilities and network effects as new sources of scale beyond national markets.

Banking Dynamics in China

Younger consumers are driving changes in banking globally, but nowhere are these dynamics more evident than in China, where tech giants are challenging incumbent banks by using formidable ecosystems to attract younger users.

Their user numbers are an existential threat to traditional financial services.

Tech giants have used a combination of investment in digital technologies and ecosystem orchestration to seize the emerging opportunity. Ping An, which was once a traditional insurance company, has built a large customer and supplier base by targeting underserved needs. It has invested \$1 billion a year in tech innovation and has spun off four major platforms—focusing on reward points, car and house sales, peer-to-peer trading, and wealth management—in an IPO.

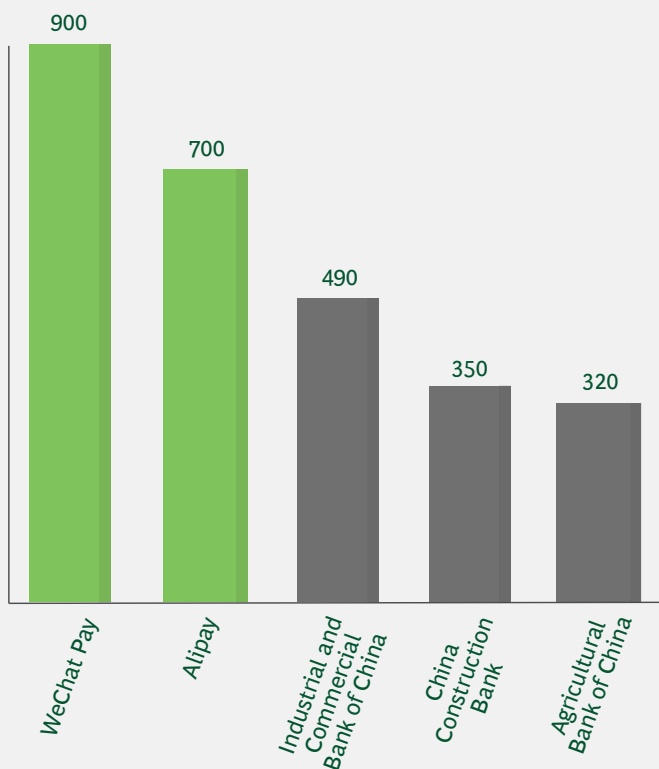
WeChat, part of the Tencent empire, invested \$2.5 billion a year in flexible, highly scalable systems that leverage customer data and advanced analytics to develop new features. It has major platforms in money transfer, e-commerce, in-store payments, and wealth management.

Ant Financial, which was started by Alibaba as Alipay in 2004, has grown into one of the world's largest financial-services firms with offerings that run the gamut from payments to money market funds to consumer and small-business credit.

Big Techs have the customer base to rival huge Chinese incumbent banks

Younger users are driving the shift toward a digital banking future

Number of retail bank customers or active users in 2018 (millions)

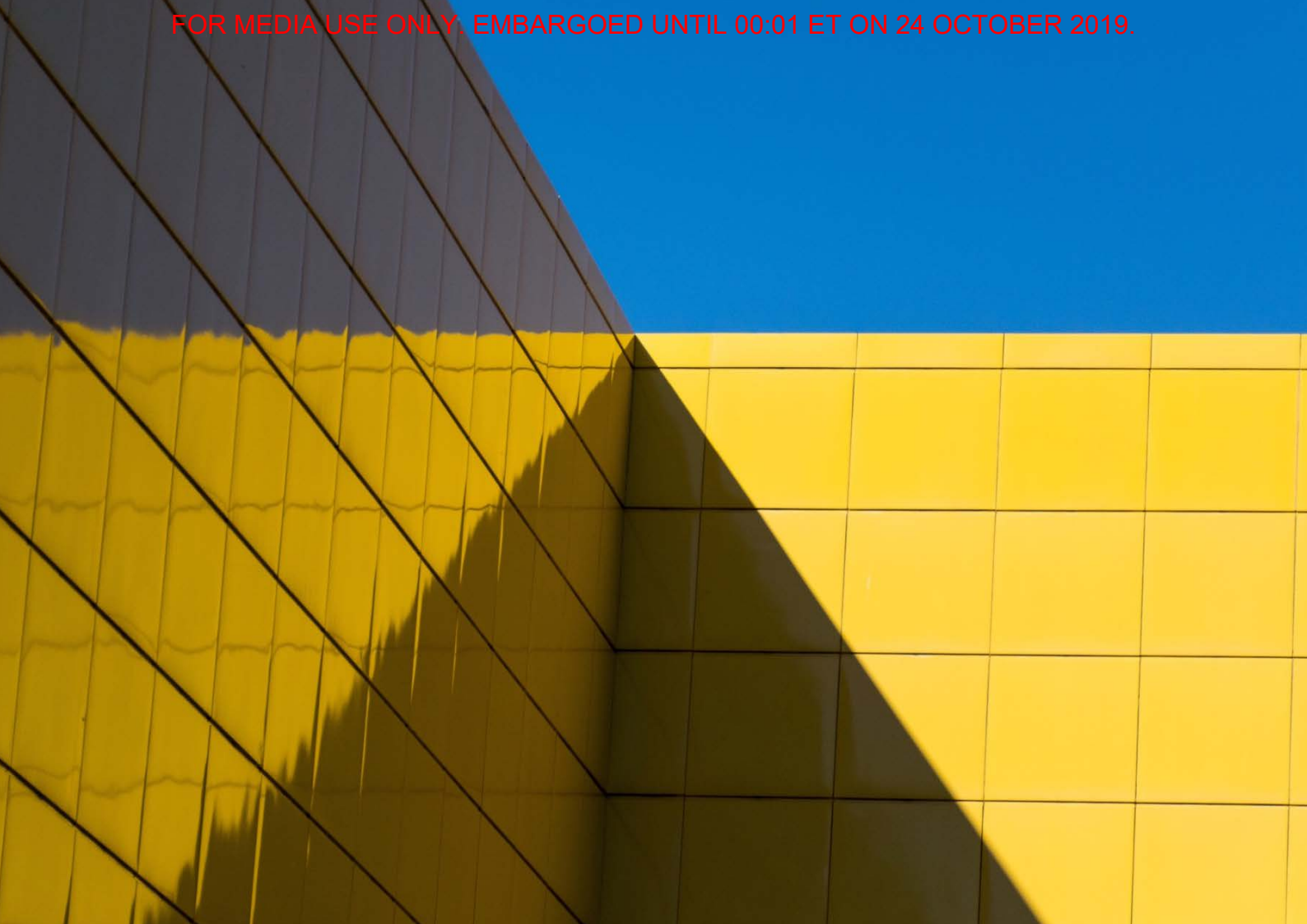


Sources: Company annual reports; BCG analysis.

Top five Chinese banks' credit card user base

WeChat user base





The New Battleground

Relevance and Scale

Banks face a new fight for consumer relevance and scale—relevance meaning the ability to offer ubiquitously available banking solutions and scale being about the number of customers banks can hold onto in the face of nontraditional competition. Incumbents have considerable advantages, but their new competitors bring substantial strengths of their own. Incumbents face the dual challenge of battling both their peers and the new entrants for consumer relevance and scale.

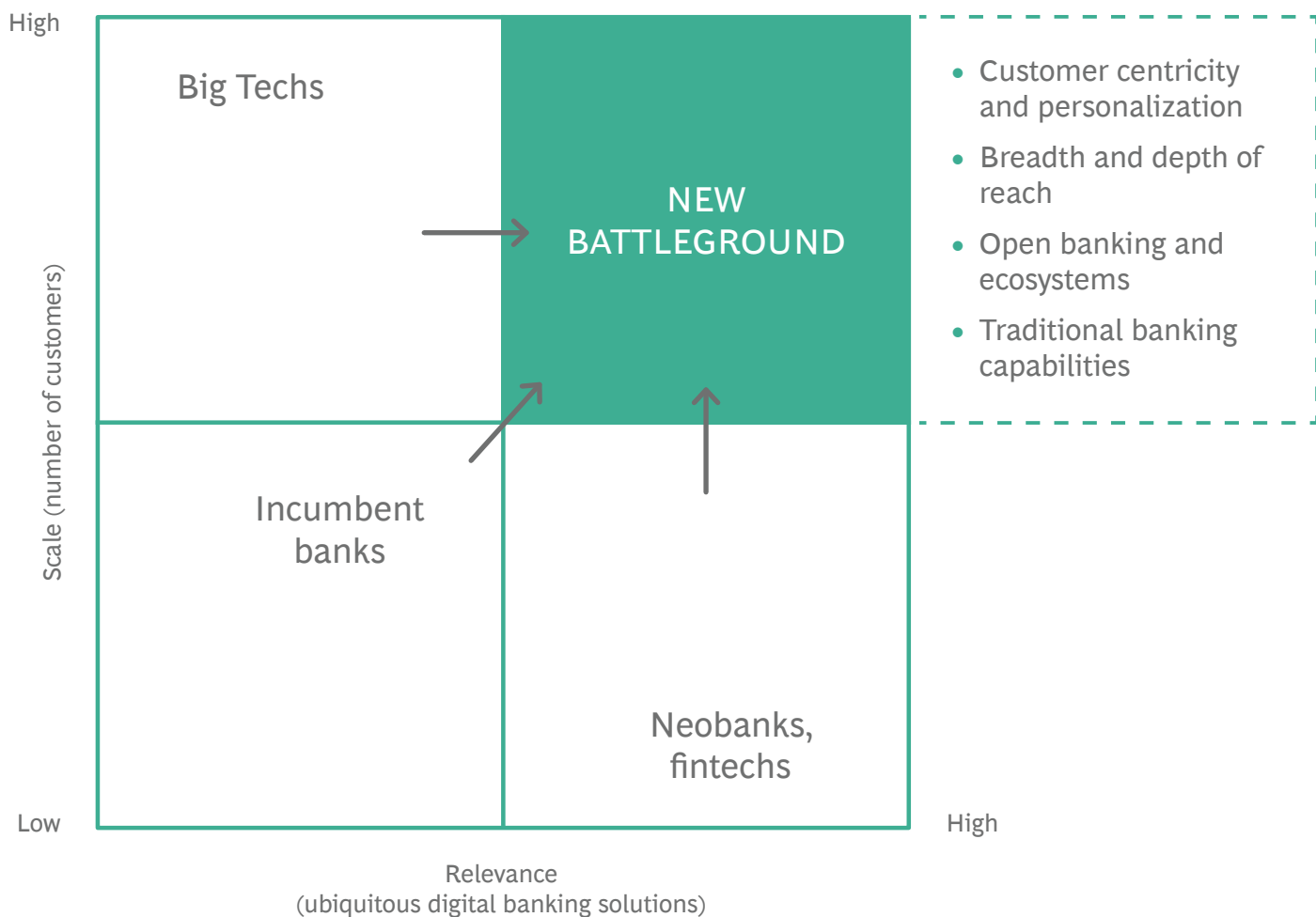
To win in the new battleground, new skills are required in addition to traditional banking capabilities:

- Customer centricity and personalization—the ability to develop and deploy innovative solutions for unmet needs will become increasingly essential, as will being able to engage with customers as individuals at scale.

- Breadth and depth of reach—scale, in terms of the number of customers, will be a defining attribute.

- Open banking and ecosystems—open, scalable platforms operated in collaboration with other third parties to develop relevant products and services will become more and more prevalent in financial services.

New Success Factors to Achieve Relevance and Scale

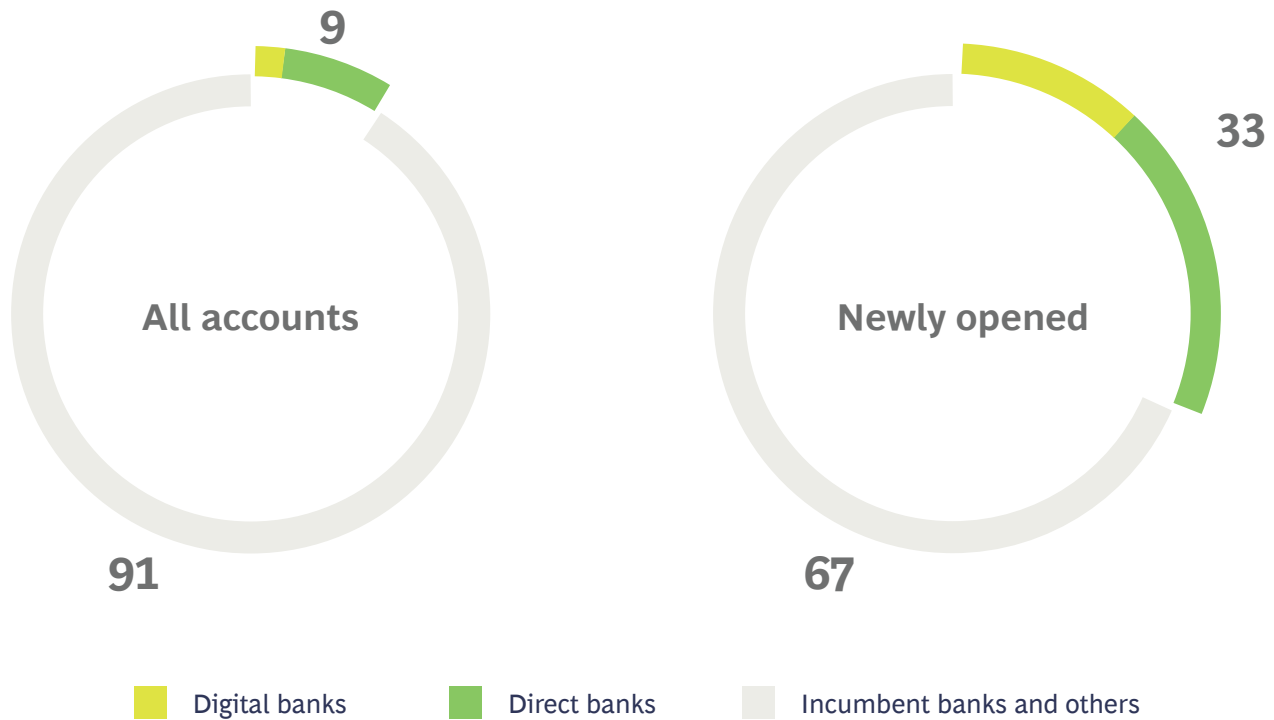


Source: BCG analysis.

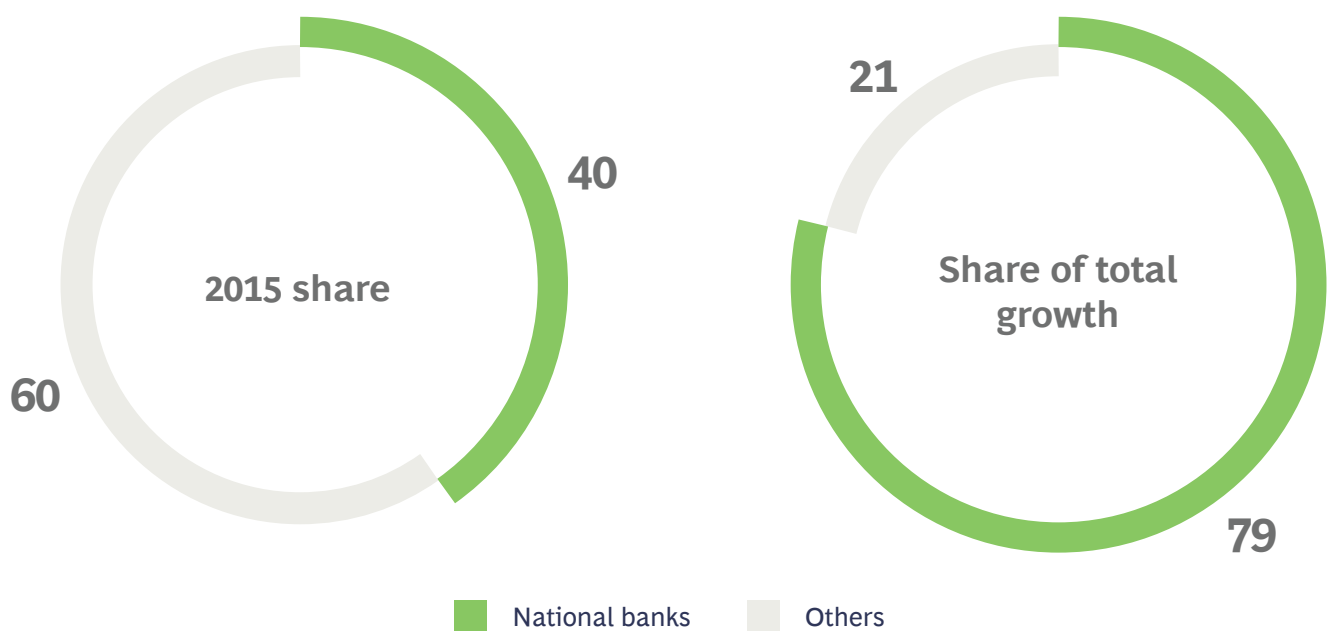
It's Happening Faster Than You Think

Digital banks are already making big inroads in major markets. For example, our estimates show that neobanks' and direct banks' combined share of newly opened accounts in Germany is three times their share of existing accounts. In the US, large banks have used their scale advantage to invest heavily in digital, and this has helped them to increase their market share.

Current accounts in Germany, 2018 (%)



Share of US transaction deposit volume, 2015 and 2015-2018 growth (%)



Sources: German Central Bank; Federal Reserve Board; corporate websites; BCG analysis.

How Will the Future Take Shape?

The pace of disruption will differ by market and so will incumbents' responses. Because the attackers operate more efficiently than incumbents, they have a margin advantage. The larger the share won by the challengers, the stronger the margin compression, as we show in scenarios two and three below. At the same time, banks lose share to their new competitors. Depending on the assumptions one makes, the role of incumbents in retail banking could change fundamentally compared with today. We see three scenarios.

Incumbents lead banking in the future. Banks invest heavily in technology to provide increasingly digital, personalized, omnichannel offerings. Challengers fail to make significant inroads. In this scenario, the future looks quite similar to the status quo—banks retain their current position by doubling down on digitizing business and operating models.

This outcome is most likely in relatively small markets with a limited number of strong and already well-digitized banks that are not high on the target list of Big Tech. Consumers tend to trust hometown players, and markets are protected by local regulations. These conditions could apply to markets such as Norway.

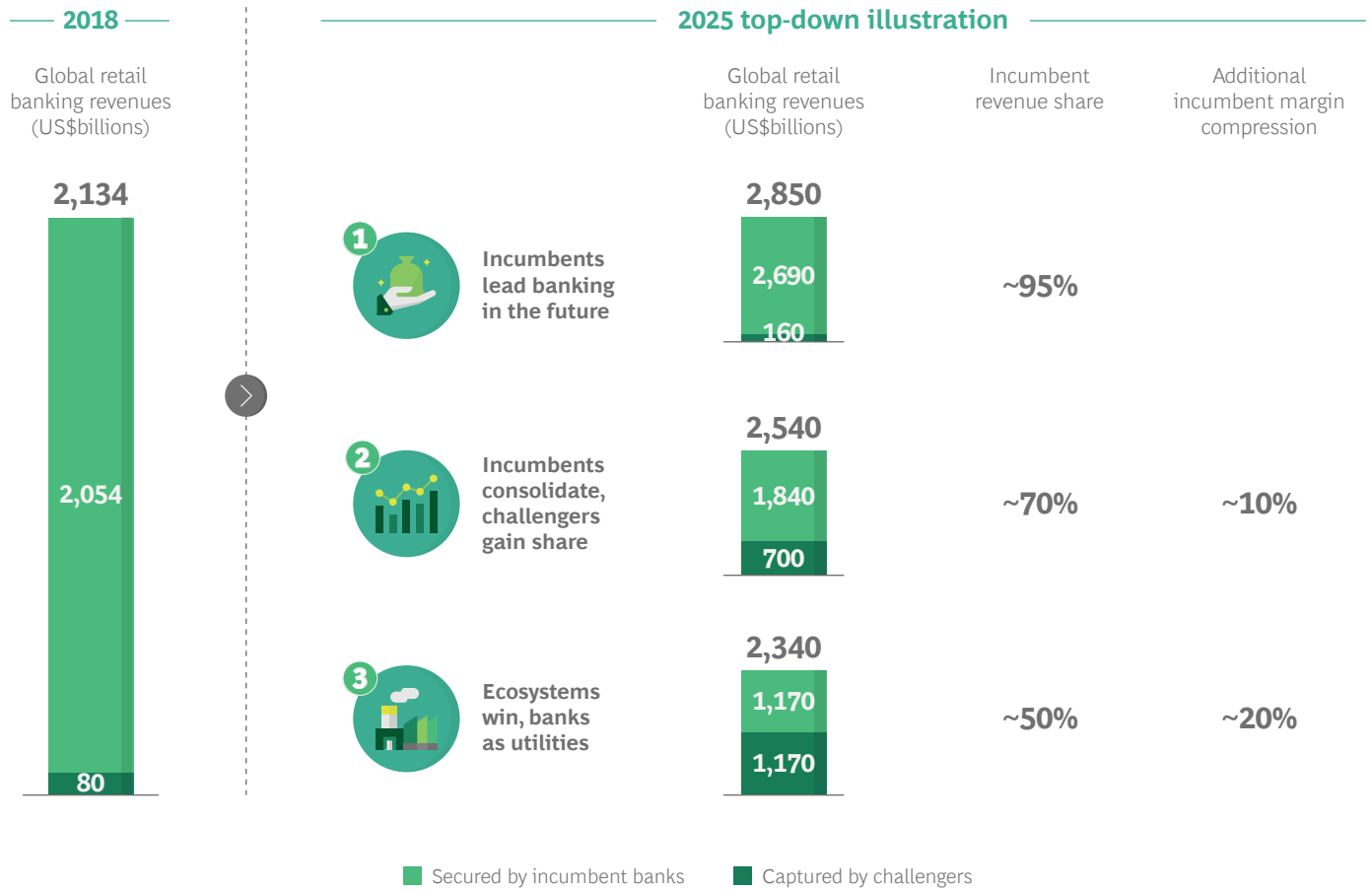
Incumbents consolidate, and challengers gain share. Digitally advanced banks compete by building new capabilities and relevance with customers. They outperform digital laggards, drive consolidation, and take up the fight with tech giants. Challengers nonetheless capture significant share through their customer ecosystems. The industry becomes much more modular, with high B2B collaboration (both vertical and horizontal).

This scenario is most likely in medium to large markets with a combination of major incumbents and active insurgents. The US is the leading candidate. High numbers of digitally savvy and traditional customers facilitate this scenario. The pace of consolidation in each market is determined by the speed and penetration of digitization.

Challengers win. In this scenario, challengers provide a superior customer-centric experience. Banks become pure utilities—that is, providers of accounts and renters of balance sheets. They provide mostly lending and deposits through the challengers' channels. The industry becomes orchestrated by marketplaces, likely run by the tech giants. Banks no longer own the customer interface.

This scenario is most likely in markets with very fluid structures and few dominant and well-digitized banks, a high availability of funding for new ventures, and a regulatory environment that promotes competition from challengers. Consumers trust the new players to meet their needs, or the market has a high share of unbanked or underbanked people. Either way, consumers seek digital solutions at a low cost. China is the most prominent potential example of this scenario.

Future Paths



Sources: BCG Banking Pools, BCG analysis.

**For most banks, the
open bank option may
be the best choice**



The Options for Incumbents

Incumbent banks need to rethink their strategies and the business models they want to pursue in the emerging industry landscape. We see four viable options emerging to various extents in different markets.

Incumbent Options



Possible evolution of incumbent business models

Digitized full-service banks

In this model, vertically integrated banks offer a proprietary catalogue of their own products through their best-in-class digital channels and branch network. While this might seem to be no more than the evolution of the current incumbent business model, it actually requires a fundamental digital transformation and a vast simplification of products and end-to-end operations. Only when they become fully digital organizations will banks be able to compete with new players that are born with the capabilities required to succeed today.



Open banks

These banks build and distribute their own products to their own customer base while they simultaneously expand their reach using distribution allies and enhance their offerings through product and service partners. This is a highly digitized model that requires the capability to connect with distribution and product third parties seamlessly. Distribution partners become a new channel that needs special management and could well compete with a bank's captive channels. Similarly, sourcing from other companies requires very different capabilities than typical procurement activities today. Intense customer focus is critical for this model.



Ecosystems

In an ideal world, a full-service bank would be the platform for products and services provided by an extensive network of partnerships, including companies from outside the industry, that have offerings relevant to the banking customer's buying journey. As with open banks, this model requires seamless integration with partners and the ability to capture and share data from multiple sources to provide customer value. Owing to the nature of network effects, the number of ecosystems for each set of customer needs in a particular market is limited, which tilts the playing fields toward early movers that get things right. Players from various industries will also fight to be the center of gravity, or **the orchestrator, of these ecosystems**. Banks need to ask themselves whether and how they are best suited to win as an ecosystem player.



Product engines

In this model, banks act as manufacturers of best-in-class products that are distributed mainly through third-party channels. They prioritize investments in the product platform—and accept the risk that they may lose relevance at the customer interface—because they recognize that becoming the partner of choice for the customer interface winners is the better investment. This role requires product excellence at a highly competitive delivery cost.

In addition to these four models, banks should consider investing in new digital growth opportunities themselves.

New digital growth

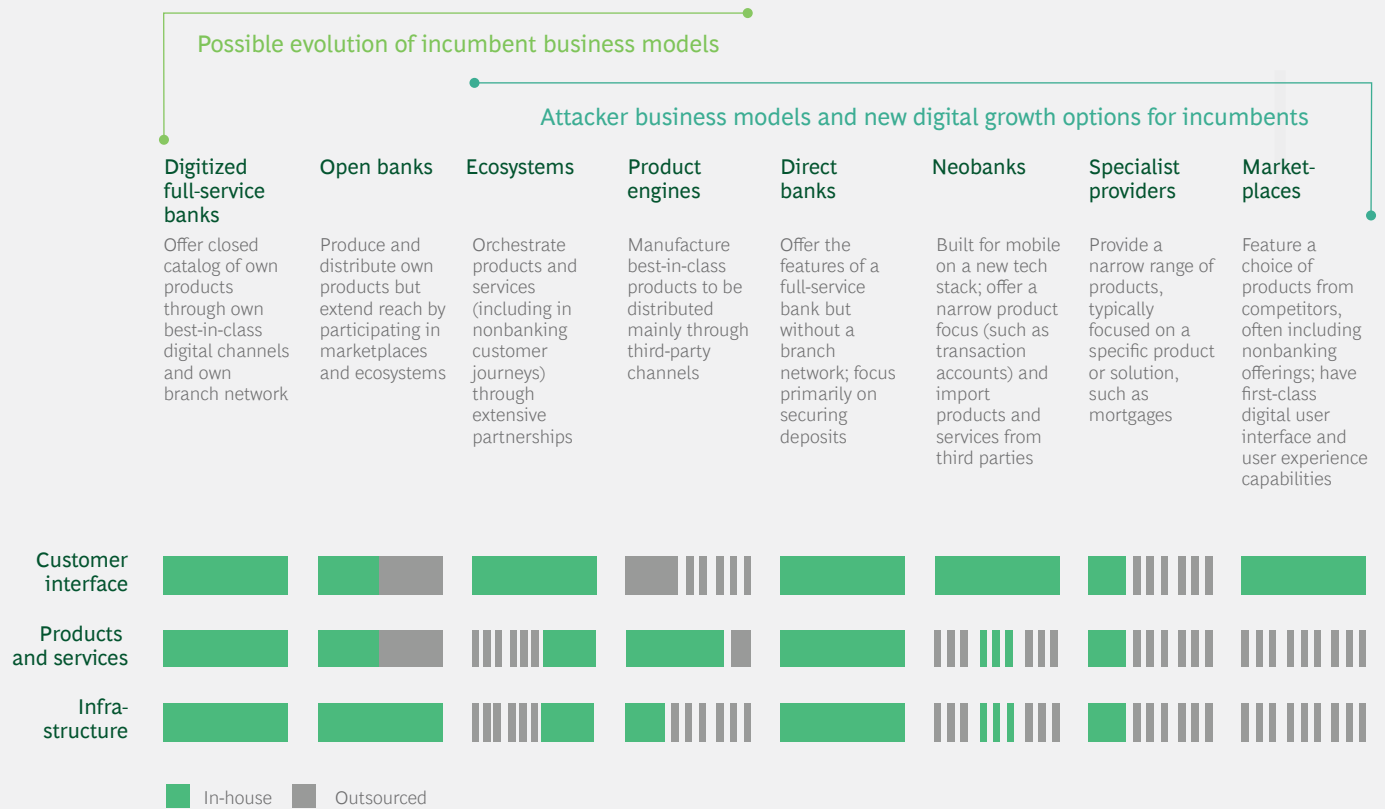
Source: BCG analysis.

A Spectrum of Digital Models

This full range of digital models is available to both incumbents and insurgents; some are evolving from traditional banking practices, while others are the product of new entrants' innovations. Banks need to assess which models

hold the most promise for them on the basis of expected changes to their markets and their own capabilities and aspirations.

Detail: full set of future business models for incumbents and attackers



**Move now—or lose out
later**





Build New Capabilities Now

Incumbent banks need to set their strategy, which will be determined by their starting point and the conditions in their markets.

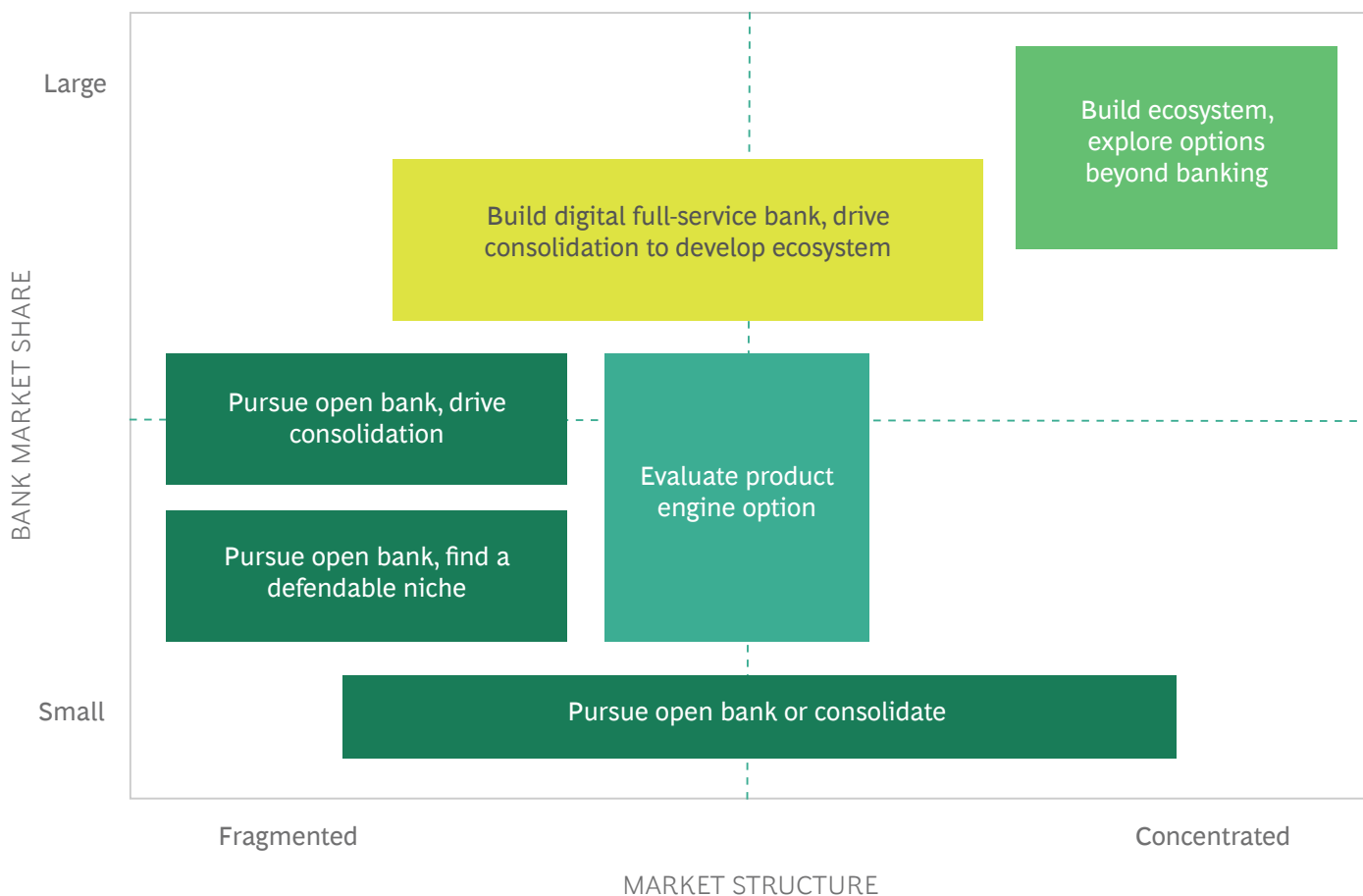
Banks with a large share in concentrated markets have the best chance to succeed with an ecosystem strategy. They should invest to sustain their current position and expand their relevance for customers. Not all banks will succeed in all segments. Banks need to evaluate where the odds are best given their customer base and capabilities today as well as the potential competition from other banks and new entrants in the future.

Some banks, especially the ones with good shares of moderately concentrated markets, have the size to invest in the digitized full-service bank model. They can also drive consolidation to achieve greater scale and increase their chance of building successful ecosystems. Their most likely competition will come from players in other industries that have stronger customer relevance.

For most banks—meaning those with smaller shares in fragmented markets—the open bank option may be the only viable way to secure relevance. They lack the scale to orchestrate an ecosystem or to invest in the digitized full-service model. Stronger and larger banks should actively drive consolidation. For smaller banks, pivoting toward niches—be they customer segments, geographic areas, or specific products or services—will be an option as well.

For banks with decent shares in larger markets that are willing to let go of the customer interface, building a product engine is a potential option, especially if they have a superior technology and operations platform today.

Each bank needs to set its strategic direction, depending on the starting point and market environment.



Getting Started

Whichever model a bank chooses, it must be clear on its value proposition for target segments as well as the business and operating model needed to deliver on that proposition. Banks can follow a three-phase approach to investing in relevance and scale.

Review the current landscape

Assess the bank's position versus current and emerging competitors. Analyze key market trends and changing customer behaviors as well as their impact on value pools. Establish what it will take to maintain consumer relevance.

Test and align on the business model

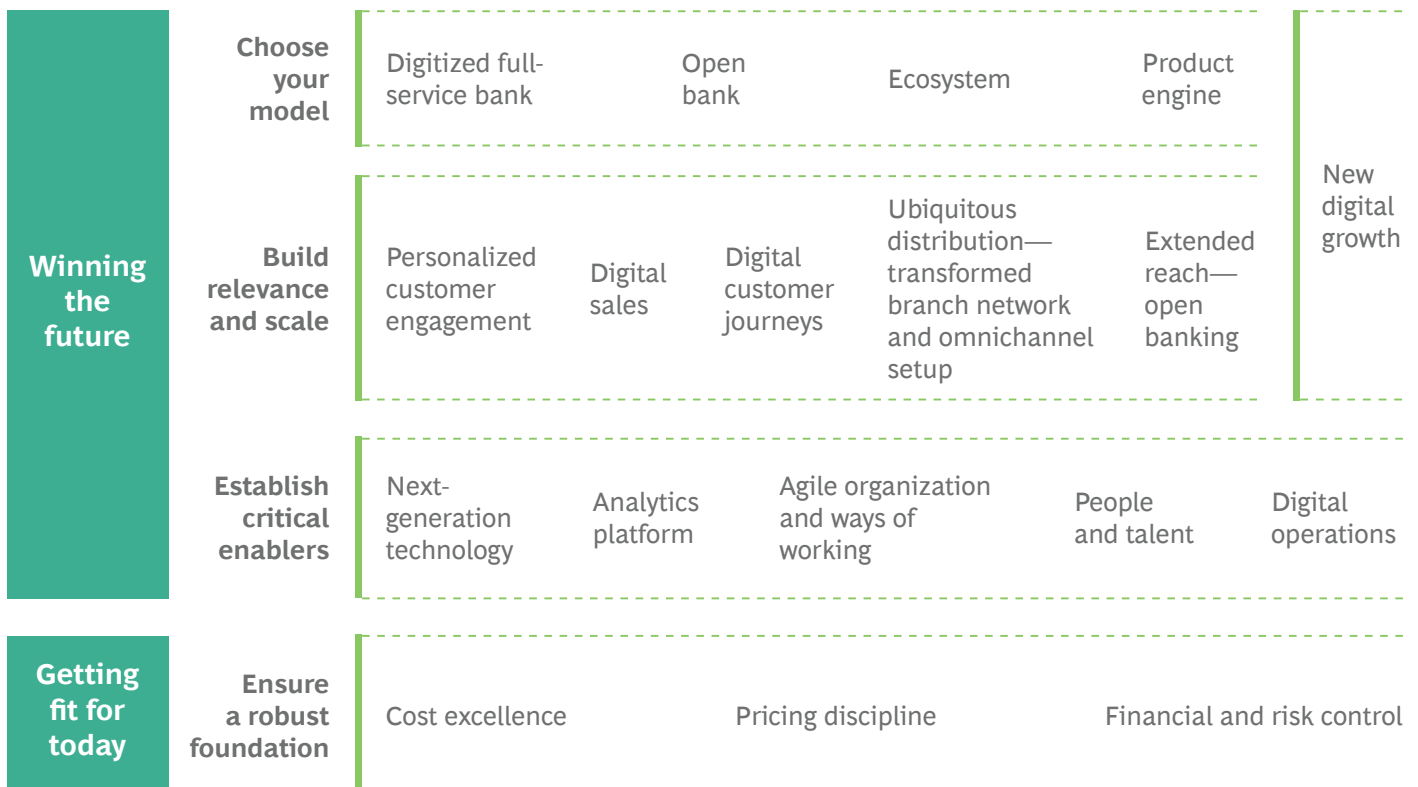
Evaluate the potential business model options on the basis of the strength of competitive advantage, the capabilities required, and the likely investment returns. Pressure test the options against likely market scenarios.

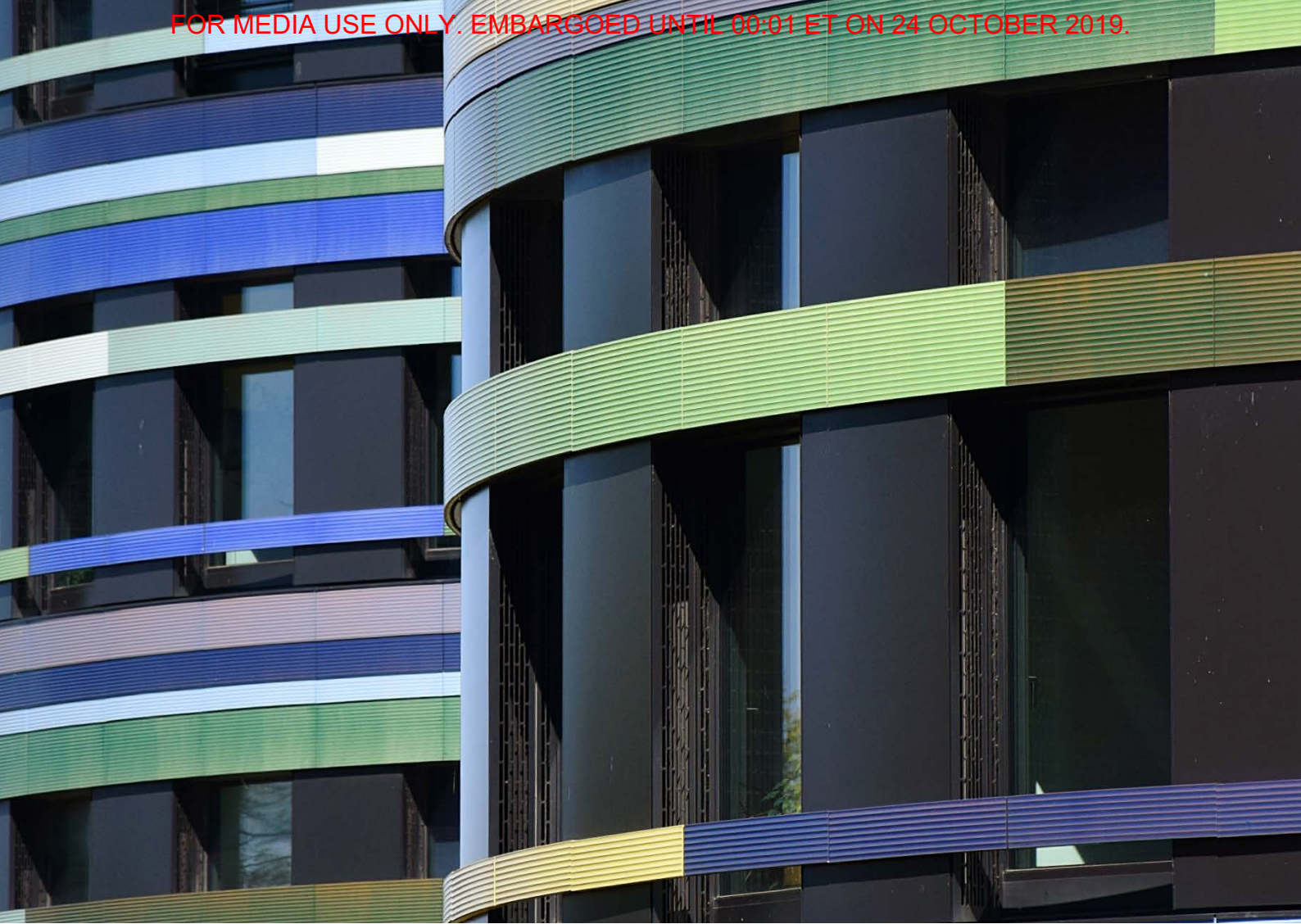
Develop a roadmap

Identify the key capability gaps. Prioritize investment in the most important or valuable use cases. Develop sequencing of the initiatives (including a technology roadmap). Execute using agile ways of working.

Developing the Necessary Capabilities

Retail banks with the ambition to win in the future must invest in developing the necessary capabilities. These will vary depending on the business model decisions described earlier.





Conclusion

Retail banks need to find their strategy for winning in a fast-changing marketplace. A clear value proposition for a bank's targeted customer segments remains the anchor for market success. On the basis of their market position today and their strategic assets and capabilities, banks need to select their future business model—a digitized full-service bank, open bank, ecosystem, or product engine. The transformation to the new model will then require decisive leadership and investments in new capabilities.

Banks that are willing to transform can look to ambitious front-runners for direction, but no bank or new competitor has yet completed the journey. Given the unprecedented speed and extent of the changes underway, the winners of tomorrow will be the ones that dare to build for the future without knowing exactly how events will play out.

About the Authors

Thorsten Brackert is a partner and director in the Frankfurt office of Boston Consulting Group. You may contact him by email at brackert.thorsten@bcg.com.

Chaojung Chen is a managing director and partner in the firm's Tokyo office. You may contact her by email at chen.chaojung@bcg.com.

Jorge Colado is a managing director and partner in BCG's Madrid office. You may contact him by email at colado.jorge@bcg.com.

Laurent Desmangles is a managing director and senior partner in the firm's New York office. You may contact him by email at desmangles.laurent@bcg.com.

Muriel Dupas is a senior sector manager in BCG's London office. You may contact her by email at dupas.muriel@bcg.com.

Acknowledgments

The authors are grateful for insight, research, and expert support from our many BCG colleagues in the Financial Institutions practice. In particular, we are grateful to Petra Demski, Antoine Dumortier, David Emmerman, Trina Foo, Jeewan Goula, Alasdair Keith, Paul Rataul, Michael Schickert, Dong Han Shin, Steph White, and Jungeun Woo. The authors are also grateful to Philip Crawford for marketing support and David Duffy for writing assistance. They thank Katherine Andrews, Siobhan Donovan, Kim Friedman, Abby Garland, Frank Müller-Pierstorff, and Shannon Nardi for editorial and production support.

Pierre Roussel is a managing director and partner in the firm's Paris office. You may contact him by email at roussel.pierre@bcg.com.

Holger Sachse is a managing director and partner in BCG's Düsseldorf office. You may contact him by email at sachse.holger@bcg.com.

Sam Stewart is a managing director and partner in the firm's Sydney office. You may contact him by email at stewart.sam@bcg.com.

Monica Wegner is a managing director and partner in BCG's Sydney office. You may contact her by email at wegner.monica@bcg.com.

For Further Reading

Boston Consulting Group has published reports and articles on related subjects that may be of interest to senior executives. Examples include those listed here.

[Retail Banking Distribution 2025: Up Close and Personal](#)
A Focus by Boston Consulting Group, September 2019

[What Does Personalization in Banking Really Mean?](#)
An article by Boston Consulting Group, March 2019

[Retail Banks Must Embrace Open Banking or Be Sidelined](#)
An article by Boston Consulting Group, October 2018

For information or permission to reprint, please contact BCG at permissions@bcg.com.

To find the latest BCG content and register to receive e-alerts on this topic or others, please visit bcg.com.

Follow Boston Consulting Group on Facebook and Twitter.

© Boston Consulting Group 2019. All rights reserved.

10/19

