The Future of Banking is Open

Open banking

What it is, why it matters, and how banks can lead the change

If a consumer wants to block out the world around them, a single app gives them access to hundreds of thousands of songs and podcasts; over time, this app learns about their tastes and suggests new tunes for their listening pleasure. As technology evolves and artificial intelligence becomes more pervasive, consumers are beginning to ask why managing money cannot be as intuitive as managing music?

Data is a key ingredient in offering personalized financial services, but it has been traditionally hard for consumers to share sensitive information with third parties, in a secure and consistent way. In response, financial innovation globally by both traditional and emerging players has taken place. This has led to an increase in financial innovation globally that is driven partly by the market and partly by regulation.

As the world responds to the COVID-19 pandemic, one of the clear outcomes is accelerated digital engagement, something that can only be done quickly and at scale through an open ecosystem and the unbundling of financial services.

In this paper, we look at what open banking is, the way some of the world's most forward-thinking banks are responding, and how Visa Consulting & Analytics can help in transforming your business.

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What is open banking, and why does it matter?

Broadly put, the term open banking refers to the use of APIs (Application Programming Interfaces) to share consumers' financial data (with their consent) to trusted third-parties that, in turn, create and distribute novel financial products and services.

A primary objective is to empower consumers and ensure consumer choice. In addition to putting consumers at the heart of the financial ecosystem, open banking should encourage innovation, with more players entering the ecosystem to create more tailored and relevant financial products and services.

Open banking can bring three big potential benefits to consumers:

More effective competition

As it becomes easier for consumers to make like-for-like comparisons on price and service, and for more competitors to enter the market.

Increased innovation

As collaboration accelerates between traditional banks and new players.

A better consumer experience

As new players emerge to optimize the value chain, especially if they can implement robust security standards.

What is driving open banking?

Open banking is driven by four market forces:

TECHNOLOGICAL TRANSFORMATION

The pace of technological change has never been faster.

Today, computing is more abundant, affordable, and advanced than ever. At the same time, ubiquitous connectivity, smart devices and pervasive mobile coverage mean that consumers expect to access convenient, engaging experiences and services anytime, anywhere.

In addition, advances in analytics means that data can be interrogated in near real-time and can provide incredibly accurate conclusions about people's wants, needs, and preferences.

Meanwhile, there is a move globally towards Real Time Payment networks, which can make account-based payments smarter and faster than ever before.

CONSUMER EXPECTATION

The weight of consumer expectation has never been heavier.

Spending upwards of five hours a day on our mobile devices, we are used to super-convenient, always-on, any-place, friction-free propositions.

An army of both digital giants and upstart challengers have a laser-like focus on the consumer experience. They are using the data generated by consumers to gain a deeper understanding of behaviors, preferences, and values to create personalized solutions. And, as consumers, we are coming to expect the same quality of service and degree of personalization in all of our dealings.

COMPETITIVE PRESSURE

The level of competition in financial services has never been keener.

The big change was the emergence of the Fintech sector as well as global digital giants, with hundreds of millions active users, moving into financial services. This new breed of lean and agile providers is delivering better consumer experiences, using digital in a more consumer-centric manner, unencumbered by legacy infrastructure issues or hindered by traditional banking regulation.

REGULATORY CHANGE

In some countries, policymakers have proposed regulatory frameworks that envision financial institutions providing third parties with access to certain information based on consumer consent.

Under these circumstances, the ability to anticipate regulatory change and move swiftly to accommodate it is no longer just a legal and compliance requirement but a source of competitive advantage.

In the European Union (EU), for example, banks are mandated to transition to open banking. Across the region, registered third parties can request access in two ways described below.

This means new products and services are likely to involve two new types of players or, in some instances, a single player delivering both services:

Types of access	Third party player objective	Terminology
Access consumer banking information – for example, to help them manage, analyze, and plan their finances better.	Drive consumer ownership	Referred to as an Account Information Service Provider (AISP) in the EU.
Allow third parties to initiate payments from consumer qualifying accounts.	Reduce friction, and capture a share of the payment ecosystem profit pool	Referred to as a Payment Initiation Service Provider (PISP) in the EU.

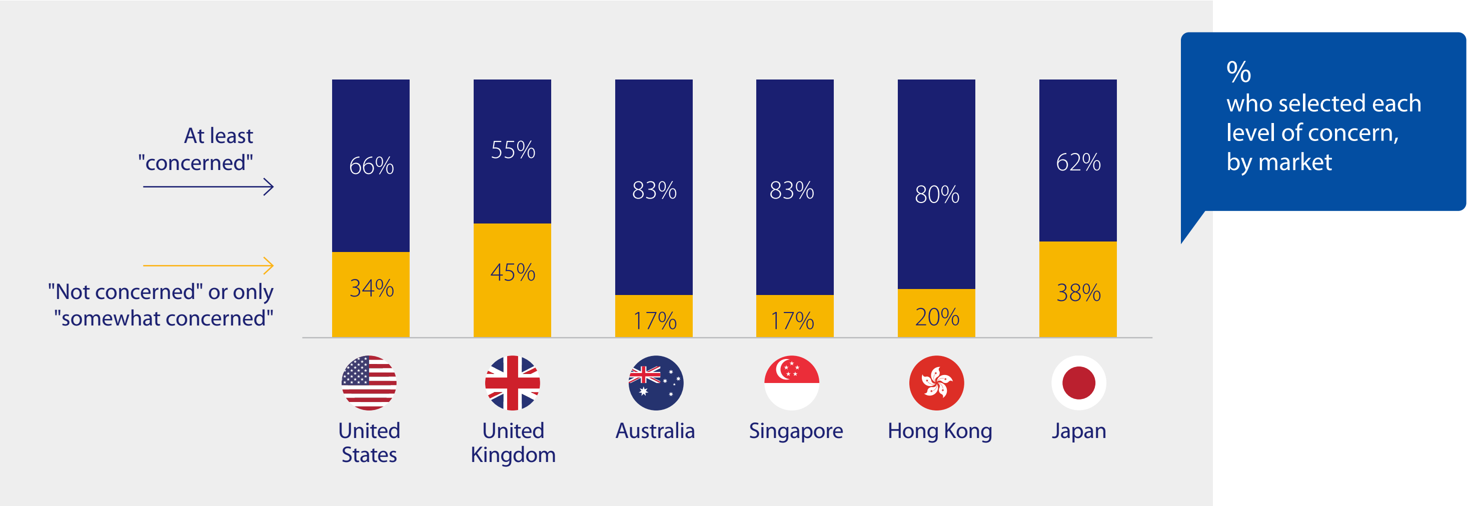
What are the consumer considerations?

The approach of regulators and the actions of banks mean very little unless consumers have an appetite for the changes and are enthusiastic about the products and services.

In this regard, a potential barrier to the uptake of open banking is consumer trust. More specifically, consumers need to feel satisfied that any third parties accessing their account information are trustworthy. This is generally tied to data privacy concerns.

To get a better sense of such data privacy concerns, Visa commissioned a number of in-depth research programs. Around the world, we can see that more than half of all consumers are concerned about the privacy of data shared digitally *(see figure 1)*.

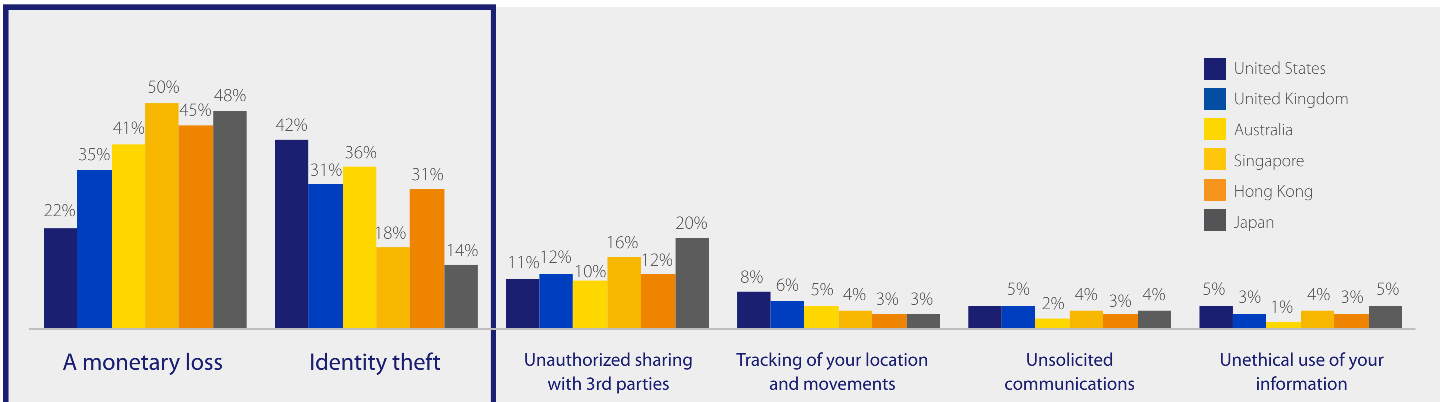
Figure 1: Concern regarding privacy of information shared when conducting digital activities



Source: Visa/A.T. Kearney 2019 Data Privacy Study (U.S. N=5,215, U.K. N=5,252, AUS N=800, SG N=1,000, HK N=1,000, JP N=2,500)

Dig deeper into the data, and the risks of identity theft and monetary loss emerge as the main concerns *(see figure 2)*.

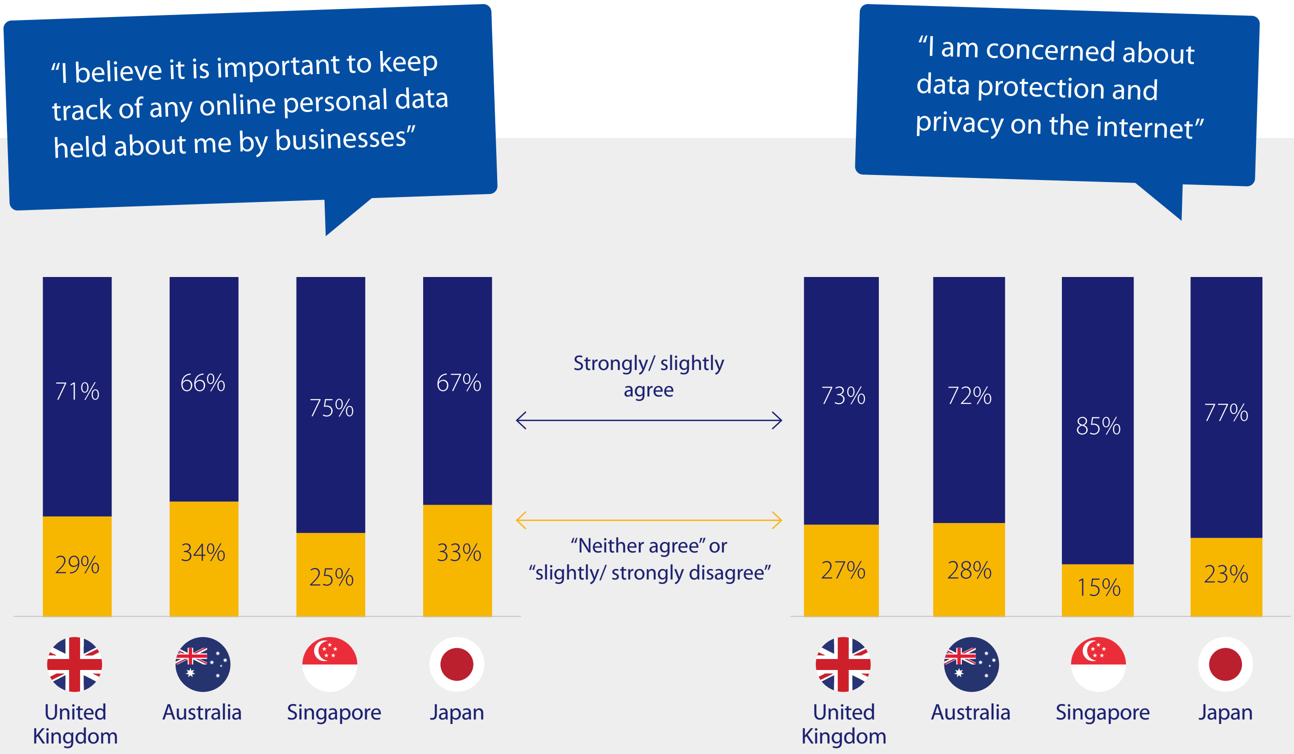
Figure 2: Main concern regarding privacy of information shared when conducting digital activities



Source: Visa/A.T. Kearney Data Privacy Study (U.S. N=4,852, U.K. N=4,765, AUS N = 500, SG N=967, HK N=958, JP N=2,275)

Importantly, this is a global preoccupation. Wherever we look in the world, it is a pressing concern *(see figure 3)*. At an ecosystem level, this issue needs to be addressed if open banking is to reach its full potential. On an individual provider level, it is a clear opportunity to differentiate services and provide added reassurance to consumers.

Figure 3. Importance of tracking online personal data held and concern about data protection and privacy

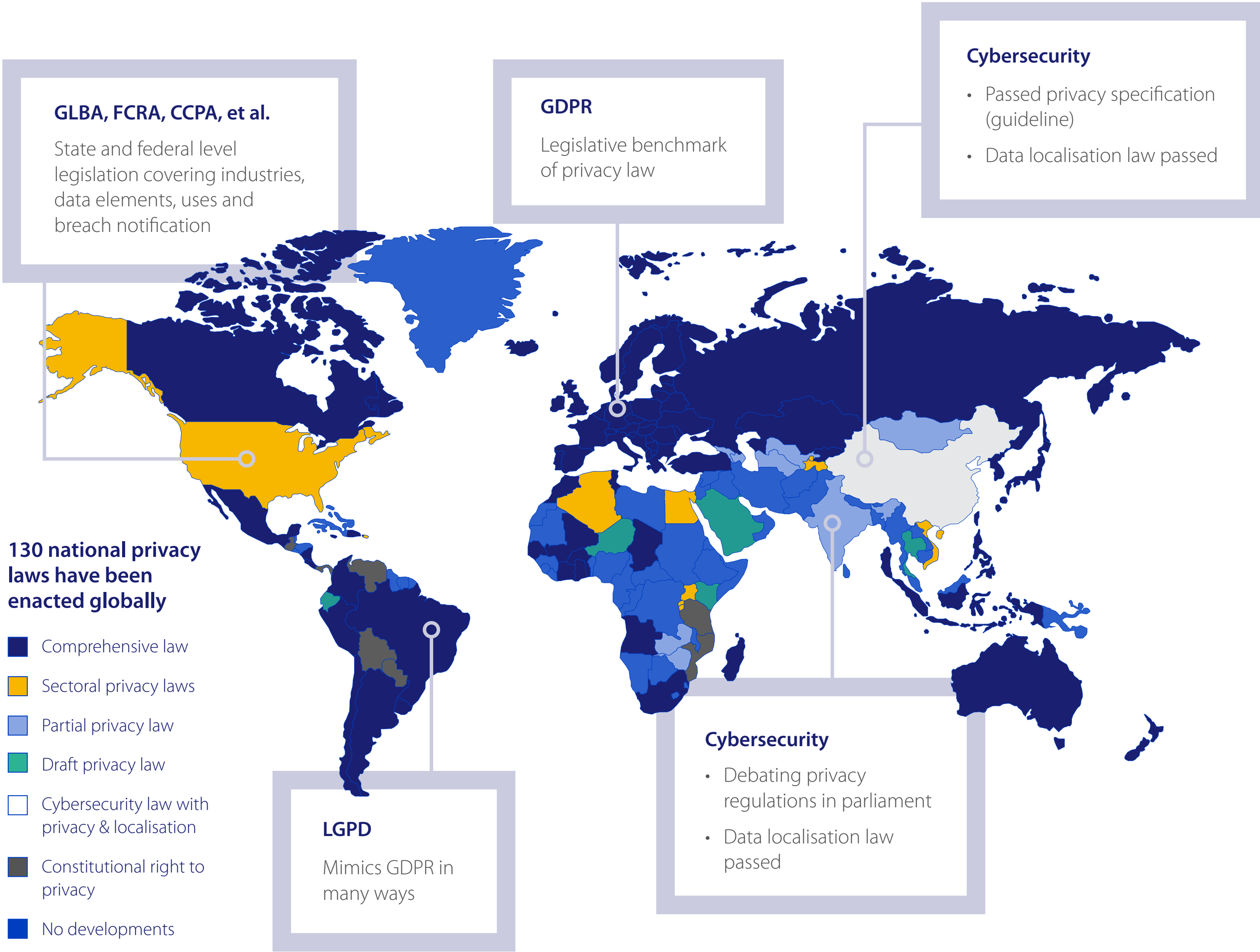


Source: Kantar Global MONITOR (U.K. N=1,000, Australia N=1,000, Singapore N=1,000, Japan N=1,000)

Reflecting this level of consumer concern, data governance is also an area of regulatory intervention. In the EU, for example, the General Data Protection Regulation (GDPR), which came into force in 2018, was the first comprehensive, enforceable regulatory framework. The aim is to give consumers rights over their own data (including the right to be forgotten and the right to access).

Meanwhile, in the US, privacy remains governed by a patchwork of federal and state-level regulations. At Visa, we see a likely increased focus by policymakers on privacy-related issues. For instance, regulation has been passed in California and multiple proposals are being evaluated in Congress. *(See Figure 4)*

Figure 4: Consumer Data Privacy regulation around the world



Source: GDPR: https://eugdpr.org/; CN: http://www.gov.cn/gongbao/content/2011/content_1918924.htm; AU: https://www.oaic.gov.au/engage-with-us/submissions/consumer-data-right-cdr-exposure-draft-legislation-submission-to-the-treasury; India: https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=11244; LGPD: https://www.lgpdbrasil.com.br/; GLBA: https://www.fdic.gov/regulations/compliance/manual/8/viii-1.1.pdf; FCRA: https://www.ftc.gov/enforcement/rules/rulemaking-regulatory-reform-proceedings/fair-credit-reporting-act; CCPA: https://www.caprivacy.org/

The good news for banks is that consumers typically view financial institutions as the most responsible actors to manage data, followed by regulators and payment networks.

This was a key finding from research commissioned by Visa and conducted in 2019 by AT Kearney. However, banks do need to carefully consider data privacy concerns and ensure they have the right data access, governance and principles in place.

From the Visa perspective, trust in the institution, consumer education and consent, along with the ability to transparently monitor and control use of data, are critical pillars to ensuring the success of open banking. In this regard, the words of Visa founder Dee Hock look remarkably prophetic – ringing true some 50 years after he first said them.

> "The ability to receive, utilize, store, transform and transmit data has expanded literally beyond comprehension.
>
> Understanding and wisdom are largely forgotten as we struggle under an avalanche of data and information.
>
> This industry is built on trust. People have to believe they can trust this way of doing business.
>
> —Dee Hock, Founder and former CEO, Visa

What are the commercial implications for ecosystem players?

Initially, many in financial services saw open banking as possibly enabling dis-intermediation of traditional banking products and services by fintechs. However, now the ecosystem is beginning to appreciate that open banking also provides opportunity for traditional financial services firms to expand their offering to existing and new customers. Ultimately, "growing the pie" could be good for everyone.

	New Risks	New Opportunities
For banks	**Pressure on margins** Consumers will be better able to make like-for-like comparisons, new players are likely to emerge offering lower-priced products and services, and traditional payment revenues will be under more pressure.	**New revenue streams and competitive advantage** Banks can not only offer "data aggregation" type services, but they can also drive better credit underwriting or acquisition efficiency as they already have the data. In addition, valuable brand trust and established consumer relationships set them apart from emerging players.
For acquirers	**Increased competition** As a new breed of payment initiation providers evolve that offer alternative payment solutions to merchants, acquiring is set to become a busier sector with a wider range of players and models.	**New revenue streams** Acquirers have an opportunity to broaden their role into "payment initiation" type services. As well as competing against new players, they will have significant potential to collaborate with them.
For merchants	**Significant investments** To take advantage of new types of data aggregation and payment initiation providers, significant spending will be required – in new infrastructure, technology platforms and analytics capabilities.	**Reduced cost of acceptance** With new payment initiation options available to them, the per-transaction cost of acceptance could help drive growth of digital payments as more innovation enters the market, reducing overall costs for merchants.
For fintechs	**Significant investments** To take advantage of new types of payment initiation providers, significant spending will be required – not just in technology and platforms but also to differentiate and market their solutions.	**Scope for new products and services** With open access to bank account data, Fintechs will have a direct access to consumers. Consumer demand will open opportunities for new entrants to collaborate with incumbents to drive more innovation and grow acceptance.

How are banks responding? Five strategies to consider

At Visa Consulting & Analytics, we have identified five ways in which banks can evolve their business models in line with open banking. We put the spotlight on five forward-thinking banks as exemplars.

Response #1

Enhance the traditional banking model

EXEMPLAR

HSBC

Enhance existing products and services to match those offered by emerging players

This is perhaps the most basic response.

It is about enhancing the user experience (UX) across mobile and digital channels and about account aggregation – which means you need to be bold and confident enough to include competing brands and accounts on your own channels.

A good example of this approach is HSBC. The bank offers a complete, real-time overview of the consumer's financial affairs, which includes accounts and balances, both HSBC-branded and competitor-brand.

What's next? We believe the next stage of evolution in this type of functionality is going beyond simple aggregation to deliver additional value though personal financial management tools and features.

Response #2

Banking as a marketplace

EXEMPLAR

N26

Integrate core products with third-party solutions to offer a comprehensive range of money-related services

This is a product diversification strategy, whereby banks can open up their platform to offer products and services from other complementary players (and it enables banks to package up self-contained products and services that can be sold on platforms operated by other players).

A good example of this strategy comes from N26, a German-based neo-bank, launched in 2013. By July 2019, it had exceeded 3.5 million account holders, and was adding another 10,000 consumers every day[1]. N26 has a highly optimized mobile app that is easy-to-use and functionally rich. Alongside its own accounts, it offers niche products from third parties – like international transfers from TransferWise, P2P remittances from MoneyBean, and loans from Auxmoney.

1. Business Insider, Rachel Green, Jul 19, 2019, "N26 has catapulted to a $3.5 billion valuation shortly following its US debut"; https://www.businessinsider.in/n26-has-catapulted-to-a-3-5-billion-valuation-shortly-following-its-us-debut/articleshow/70295904.cms

Response #3

Banking as a service

EXEMPLAR

solarisBank

Focus on the core infrastructure of banking services, and leave the front-end distribution to others

This is a platform play – whereby a technologically adept organization, creates an agile and highly capable core banking infrastructure, and enables other players to create and launch white-labelled banking products.

A great example of this approach is the German-based solarisBank. Calling itself a tech company with a banking license, it has raised more than EUR95 million in capital (including stakes from Unicredit, BBVA and ABN AMRO), and is said to have brought more than 20 companies onto its platform.

By offering a white-labelled platform and a suite of white-labelled products, and by taking care of the heavy burden of regulatory compliance, it offers other players a quick and simple route to launching their own challenger bank.

Response #4

Separate new bank

EXEMPLAR

Royal Bank of Scotland

Launch a separate digital-only bank to more easily drive innovation and target new consumer segments

This is a pragmatic way for established banks to escape the burden of their existing infrastructure and processes.

Many existing banks may be eager to participate in the upside. Yet they are conscious that building best-in-class UX and data analytics on top of their existing infrastructure is a huge challenge. Several have chosen to launch completely separate neo banks. This means they can be as nimble as any start-up, yet still pull on the resources and expertise of a large parent organization. It also enables them to target those consumer segments who are most likely to be attracted to a neo bank (such as millennials or small businesses).

An example is the UK's Royal Bank of Scotland (RBS). First, in 2018, it launched Mettle, a new digital-only bank created specifically to appeal to small and micro businesses. It has also announced its plans for Bó, another venture targeting younger people, and has announced plans to migrate one million existing consumers to the new bank.

Response #5

Banking as best-in-class

EXEMPLAR

BBVA

Transform by becoming an open platform with new business models supported by new capabilities

This model requires significant effort to drive a full transformation of the business.

Only a select number of large banks have attempted to take such a route, which requires them to transform their business, putting innovation at the center of their strategy. In doing so, it is necessary to redesign the business model, and then build the requisite infrastructure and capabilities.

Spain's BBVA is the prime example. Its ambition is to become an open platform by building APIs to allow other ecosystem players to access its products and services. It is also freeing itself up to tap into the services offered by other players, in order to bring the best UX and value to its own consumers.

VISA

How can Visa help you take the next step on your open banking journey?

Wherever in the world your organization is based, open banking is bound to be on your radar.

Banks everywhere can seize this opportunity, and the sooner you initiate your open banking strategy, the more success you are likely to enjoy.

Here we outline five key elements of an open banking response and how Visa Consulting & Analytics (VCA) can help.

#1

Assess your landscape – and how you fit into it

The first step is to take an unbiased look across your landscape.

At VCA, we have found that a useful discipline is to conduct a capability assessment. This can include:

- Understanding your market and regulatory environment and how it will evolve.
- Researching global trends and how they may take root in your market.
- Benchmarking products and services across the industry.
- Understanding your primary needs, opportunities and quick wins.

As part of the landscape assessment (especially in the era of open banking) it is vital to take a close look at the wider financial services ecosystem, including the Fintech community. This will help you to:

- Identify the types of partnerships that will help you realize your ambitions and build out from your pockets of unique and differentiating value.
- Arrive at a tailored, curated ecosystem view that will enable you to explore and pursue sources of additional value.

#2

Take an honest, unflinching look in the mirror

After developing a proper understanding of the market landscape, it is time to drill down further into your own organization in a self-assessment diagnostic – including your organizational structure, your channels, your portfolio performance, your partnerships, and your future prospects.

In addition to the above, a particular focus should be your existing mobile and digital apps (because, whatever the shape or nature of your open banking response, your mobile apps are certain to be the focal point). Irrespective of how sound your strategic planning may be, it will not be effective if your apps do not perform.

At VCA, we have created a framework we call Digital Banking Experience to give mobile apps the ultimate digital capability assessment and stress test. This evaluates the user experience across six key areas and 225 functionalities – enabling clients to benchmark their app against domestic and international peers as well as new players.

#3

Plan your strategic response

As part of your opportunity definition, it is useful to outline and contrast the strategic options for your future banking model and highlight the key implications (in terms of risks, investments, etc.).

It is also helpful to identify which new products and services need to be built in order to reach the end-state.

Elements to include:

Banking model – which of the five strategic responses (outlined above) is best suited to your business?

New monetization opportunities – how will you drive new revenues from new sources?

Use cases – who will use your solutions, why, and what problems will be solved?

VCA has developed a process we call blueprinting. It enables clients to define each of the required initiatives, build a business case, prioritize or heat map accordingly and, ultimately, define a strategic implementation plan.

#4

Plot your discovery-to-delivery journeys

Your strategic response will inevitably entail a series of work streams, through which you will devise, define, develop and deliver a range of new propositions.

Depending on the shape and nature of your open banking strategy you will be:

- Exploring proofs of concept
- Incubating pilots
- Commercializing set-plays

It is useful to agree to a common methodology to apply to all of these development journeys. By imposing and following a common structure, it is much easier to manage the process, monitor the progress, and keep the entire organization updated on the journey.

The evolution of the Digital Banking Experience will loom large in the journeys – which is likely to involve new API requirements, as well as new partnerships. At Visa, we have innovation centres around the world where our design teams can work with you on these challenges.

#5

Watch your performance closely – with a particular emphasis on your attrition risks

As part of your planning, you will have put together some meaningful targets and KPIs. A particular area of focus should be your attrition performance – because, as the open banking story unfolds, an entirely new attrition dynamic is likely to emerge.

You should therefore identify which consumer segments are most at risk and put an early warning system in place to predict and prevent dormancy.

At VCA, we use a predictive model based on a sophisticated AI technique, which scores consumer accounts according to their likelihood of going dormant over the subsequent six months, and enables you to prioritize your actions accordingly.

Armed with a realistic understanding of your attrition risks, you are better placed to determine your response – for example by enhancing your existing propositions, developing new propositions, or maybe even following the lead of an organization like RBS and creating a segment-specific brand or organization.

Working together to embrace the benefits of open banking

Open banking is a trend that is taking hold globally. Although it could be uncomfortable for some incumbents, the impact should be positive – both for consumers and for the financial services ecosystem thanks to a better consumer experience, keener competition, and increased innovation.

For help addressing any of the imperatives above, please reach out to your Visa Account Executive to schedule time with our Visa Consulting & Analytics team or send an email to **VCA@Visa.com**. You can also visit us at **Visa.com/VCA**.

About Visa Consulting & Analytics (VCA)

We are a global team of hundreds of payments consultants, data scientists and economists across six continents. Our consultants are experts in strategy, product, portfolio management, risk, digital and more with decades of experience in the payments industry. Our data scientists are experts in statistics, advanced analytics and machine learning with exclusive access to insights from VisaNet, one of the largest payment networks in the world. Our economists understand economic conditions impacting consumer spending and provide unique and timely insights into global spending trends.

The combination of our deep payments consulting expertise, our economic intelligence and our breadth of data allows us to identify actionable insights and recommendations that drive better business decisions.