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KPMG Perspectives

Big tech and the banking industry: Threat or opportunity?

Pressure from more than fintechs

THE banking industry faces threats on multiple fronts. Recent quarters have seen not only the rise of challenger banks in global jurisdictions, but also an increasing number of large financial technologies like Square and Klarna applying for banking charters. Yet, while these growing players have made headlines, technology and e-commerce giants like Amazon, Google, Facebook and Apple may pose greater threats to the traditional banking model.

Customer focus driving encroachment from e-commerce giants

FOR e-commerce firms like Amazon and Alibaba, the focus on creating a frictionless, one-stop shop for digital purchases is driving their entrance into areas traditionally dominated by financial players. Identification, verification and trust-based kite marks are increasingly on these firms' radar, under the banner of KYC. E-commerce giants already hold and process significant volumes of customer data. By creating their own algorithms and verification processes, these companies can achieve greater efficiency while reducing costs compared to obtaining these services from a third-party provider.

As an example, Amazon entered the lending market with Amazon Lending in 2011. Since then, more than $3 billion has been lent to small businesses in the United States, the United Kingdom and Japan, who sell on the Amazon platform.

While Alibaba and Amazon's strategies are arguably the most developed, using customer data to better manage credit risk, working capital and liquidity, other e-commerce players are investigating similar approaches. Though the focus is currently on creating an exemplary experience for customers within their ecosystem, there is the potential for such services to be offered as a white-label product in the future, further disintermediating traditional players.

Data-centric businesses apply pressure on other fronts

THE focus of technology giants like Google, Apple and Microsoft on developing and enabling data-centric business models provide threats from another front. While banks hold and process significant financial data, the speed and efficiency with which a data-centric business can achieve these same tasks is accelerating. In the future, the front-end user interface and data-processing elements of traditional banking players may eventually yield to technology players that can deliver reliable results on a more expedient timescale.

Facebook is an example of a non-fintech player expanding into what is currently fintech-dominated space: digital payments. Coming from a social-media background, Facebook's driver is the ability to monetize social communities as an integrated part of their ecosystem. While Facebook's strategy is not new, the size of its existing, engaged customer base offers opportunities unmatched by fintech or traditional payments firms.

Partnerships offer banks opportunities for modernization

DESPITE the encroachment, tech giants' growth into traditional financial-services areas offer opportunities for banking players. Current trends show that technologies, such as AI, machine learning and cloud computing will play increasingly critical roles in the financial-services industry in coming years. Partnerships with technology giants with a deeper and more robust understanding of these technologies can provide significant advantages to banks and other financial-services firms currently hobbled by legacy systems, processes and people. Increased social engagement, and technologies to better manage customer relationships in the digital sphere, offer other opportunities.

Through partnerships, tech giants can also offer advantages, such as increased speed to market, inexpensive and scalable infrastructure, and modern data-analytics capabilities, including access to proven machine learning and cognitive technologies. These are all areas in which tech and e-commerce giants excel, unencumbered by legacy technology.

China exhibits possible model for the future of retail banking

IN developed nations, despite fintech and challenger bank innovations, consumer inertia

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has left traditional players with the lion's share of personal and retail transactions—for now. Yet, in markets, such as China, a new model is developing in which digital-wallet providers aim to deliver a broad range of consumer services, of which banking and financial services are only one part. To address this threat of future disintermediation and continue to be viable as a customer interface, banks need to think more broadly about the services they provide in the real economy. Achieving this goal requires greater technological competence in accessing and managing data as an asset. In developing markets, especially in Africa and Asia, e-commerce and telecommunication firms have been able to "leapfrog" the traditional banks to offer modern banking services on mobile platforms; however, regulation and legacy infrastructure limits western banks' abilities in this regard. Diverse partnerships that offer competencies to engender similar services—whether with tech giants, e-commerce firms, fintechs or all of the above—will become increasingly critical for banks wishing to avoid obsolescence.

Looking forward

THE push of technology and ecommerce giants like Amazon, Alphabet and Facebook into financial services is driving banks to reconsider their business models and question where they fit in the changing ecosystem. Some are considering whether to focus on utility services, transaction banking or acting as a source of capital, while others are looking to become white-label platform providers of analytics, KYC and credit risk services to other firms. Each of these paths offers challenges and opportunities in equal measure. Yet, as pressures mount from a myriad of sources, it becomes increasingly clear that for banks to survive, change is mandatory.

The article "Big tech and the banking industry: Threat or opportunity?" by Jonathan Lavender of KPMG International was taken from KPMG's publication entitled The Pulse of Fintech Q3 2017.

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