La Correspondance Economique
Economic and business daily news

25 April 2016 – No 23595

Country: France
Page(s): 32-40
Surface: 639%
Frequency: Daily

Distribution: (1050)

(2 images)

La Correspondance économique
Quotidien d'Informations économiques et sociales

WEEKLY STUDY Monday 25 April 2016

Carbonnier
Lamaze Rasle & Associés
Law Practice

During a round table organised by the law firm CARLARA, Ms Marie CHEVAL, the Chief Executive Officer of Boursorama, and Mr Olivier KLEIN, Chief Executive Officer of BRED Banque Populaire and Professor of Economics and Finance at HEC, discussed the future of banking in the digital age.

During a round table organised by the law firm CARLARA led by Mr Edouard de LAMAZE, counsel at the Paris Appeal Court, partner and joint manager of the law firm Carbonnier, Lamaze, Rasle et Associés (CARLARA), Ms Marie CHEVAL, inspector of finances, CEO of Boursorama, and Mr Olivier KLEIN, CEO of BRED Banque Populaire and Professor of Economics and Finance at HEC, discussed the future of banking in the digital age.

The New Challenges

To open the discussion Mr Olivier KLEIN drew up a list of the "major challenges" confronted by retail banks. First, the regulatory challenge: the solvency ratios required have increased markedly since Basel 3. The new liquidity ratios *de facto* oblige banks to reduce loans somewhat and increase their holdings in government bonds to build cash reserves. A change that was no doubt necessary after the financial crisis but which has a disadvantage: "if growth accelerates, banks, and not only French banks, will be less able to finance the economic growth", he warned.

Secondly, banks are affected by the very low or even negative interest rates on bank deposits at the Central European Bank. "The rates margin is reducing since loan rates are falling more quickly than deposit rates", he noted, and "we cannot impose negative rates on customer deposits, especially those of individuals" to recoup the margin. To escape from this impasse "the only option will be to expand through overall market growth or acquisition of more market shares". But since the market is growing only slowly, expansion of banks overall is limited. All "this results in a reduction of the intrinsic profitability of banks", he noted.

Finally, and this was the theme of this round table, banks are confronted by a “customer revolution”, made possible by a “technological revolution”. With the Internet and related objects, customers are visiting their branches less frequently. Between 2008 and today, “visits to branches have reduced by a factor of three”, recalled Mr KLEIN, who nevertheless emphasised: “what has fallen drastically is essentially the requirement for day-to-day banking transactions, (collecting a cheque book, making an account-to-account transfer, etc.), whereas the number of added value appointments has increased”.

“Online banks are facing exactly the same challenges: regulatory, because they are banks just like any others; economic, because the rate situation has overturned all traditional scenarios; and obviously, the challenge of changing customer behaviour”, said Ms Marie CHEVAL, emphasising: “we are surfing on a powerful evolution of customer behaviour”.

The head of Boursorama set the scene for the world of digital banking. First, traditional banks have developed digital services, notably applications for distance banking transactions in response to customer needs. The “100% online banks have emerged, players such as Boursorama, frequently the subsidiaries of banking groups, with no branches”. 8% of bank customers in France say they have an online bank account. A larger proportion of customers are in “flux”. It appears that “one account in three in France is opened at an online bank” she said, to emphasise the “marked evolution of customer behaviour”.

Finally “there are new players extensively reported in the press, what I call neo-banks”. These are not banks insofar as their offer of products and services is relatively reduced (no or only small overdrafts, no savings, no loans). These are basically payment establishments evolving as part of the “FinTech” movement. “These players are responding to a need for payment services”, she said.

Banks confronted by the emergence of digital technology are organising themselves

One of the major consequences of the soaring use of digital resources is the turning away from bank counters for day-to-day transactions. “We are very happy with this development. It’s much better to have more advisers conducting sales with customers than behind the counter carrying out tasks with no added value” assured Mr KLEIN.

But the technological revolution “makes customers far more demanding of their banks”. Unless they adapt rapidly, they will “progressively be overtaken by online banks which offer greater ease of use, even if they do not offer a qualified adviser to customers, or they will be threatened because new players will disintermediate specific activities”. According to Mr KLEIN, “network banks have a bright future, but only if they take on-board all the changes required by customers” and can adapt rapidly to offer the sought-after ease of use and added value by offering high-quality advice - which obviously they have “all started to do”.

For the moment then, two types of change are on the horizon. First, "we must be far more convenient", he said, since "no-one wants to queue, to wait, to make a pointless journey, whereas with a smartphone, you can do a lot by yourself". Banks "are not paragons of virtue in terms of convenience" he acknowledged, considering that they must start by becoming much easier to contact. "To establish direct contact with a customer adviser is fundamental", he explained. Increased user friendliness also calls for improved handling of customers' requests, complaints or problems. "The customer experience must be enhanced".

A convenient bank is one where the adviser takes the initiative of contacting customers regularly: "many things are at stake here", he considered, since "proactivity is a powerful factor for the success of our banks" provided it is done "intelligently, according to the customer's needs and not simply to promote a product". Reflection on distance selling - a "fundamental" aspect – is also required. "Many customers still prefer to visit their branch and have a direct relationship when discussing major personal projects" he asserted, but those customers who prefer to deal with their affairs remotely also want "an adviser who knows them, who knows their history, who doesn't have to ask all the right questions every time they call". Finally, another aspect of convenience: it is vital to improve the customer experience. This will be achieved by making procedures less complex. "Online banks have enormously simplified opening an account, while remaining compliant" he noted. "We must do the same. This is what is happening at BRED". Another example: mortgages, where customers are informed of progress on their applications at each stage, by text or email, according to the customer's own choice and they can consult their digital casefile and if necessary, add missing documents directly online, "That will soon be happening at our bank", he promised.

In the second place, retail banks must offer "high-quality advice". Digital technology has "accentuated the need for highly-competent advisers". Why? "Simply because anyone can easily look up facts and make comparisons on the Internet, so the customer is already well informed when meeting the adviser", observed Mr KLEIN. Although this does not include "all customers", it is a trend and means advisers must step up the standard of their knowledge and skills. The aim "is not for 100% of our advisers to be 100% competent in 100% of the product range, but that 100% of our advisers must be capable of providing the desired competence, according to the type of customers they are assisting, he asserted. In brief: fine-tuning of segments is required to ensure that "the right advisers are sitting opposite the right customers".

On the other hand, Mr KLEIN "does not set much store by specialisation according to product". People don't come to see us about a product, but to satisfy a need. Any personal project - however big or small - involves savings, loans and insurance", he noted. In his view, "if you treat these topics separately, customers feel that you are splitting up their plans and losing sight of the overall vision of their projects". A high standard of advisory services also requires "a qualified adviser" who knows the customer's history, but can also call on the benefits of digital technology. Big data alone, or an adviser alone, are not optimum. But human resources plus the capacities of big data and artificial intelligence offer remarkable possibilities to advise the customer and add value for both the customer and the bank", he affirmed, pleading for a model where "distance is abolished, thanks to new technologies and human advisory capacities (enhanced by big data and artificial intelligence), placing customisation and proximity at the centre of the relationship". "This is what we at Banques Populaires refer to as the best of the human and digital worlds. A bank without distance".

Digital technology is "changing behaviour", online banks are "surfing" on these changes

And where is the online bank in all this? "It was born with the dawning of the digital age and so is native digital" emphasised Ms CHEVAL.

Digital technology is "changing customer behaviour". First of all, as already stated, it "considerably increases the overall level of demand". "When FNAC.com can deliver a book in 24 hours, you are not prepared to wait an age for a reply to your loan application, or, more precisely, you are prepared to wait - provided you know when you will have the reply", she noted, highlighting a significant change: "customers require far more information". Another point, the customer makes more comparisons. "More aware than previously", customers do not hesitate to open accounts with multiple banks. The Internet creates a very different price ratio since customers have access to a multiplicity of offers. So, customers demand "the right price for the right promise", obliging the brands to "clarify their customer promises. Ms Marie CHEVAL believes there is room for different customer promises. Another major change brought about by the Internet is "the weighting of a recommendation" with a primordial role for customer satisfaction. Online banks operate with an open architecture, giving access to all products in addition to those of their own banking group, rather like markets on the Internet.

Created at the end of the 1990s and natively with the web, online banks "surf on our behaviour". With a free bank card, a branchless bank, without dedicated advisers, at a highly attractive price, Boursorama tailored its offer of services by overturning the classic banking codes. With low tariffs, these banks generate even more revenue per customer (more recently, free bank cards etc.), but also reduced charges (no branches, autonomy). The average banking costs today in France are slightly less than €200 per annum per customer. Last year, Boursorama customers paid less than €13, said Mrs CHEVAL. "The model of online banks is to provide value for the customer".

To survive, a "simple but complete" offer is required. Savings, life assurance, but also mortgage loans". "Our credit production doubled last year. Customers enter the details of their project and obtain an "in principle" answer and a rate in real time, they can discuss concerns by phone with advisers who specialise in mortgage loans". Distance banking is not a bank without relationships, it is rather "proximity from a distance", for according to Mrs CHEVAL, "we conduct extensive relations with our customers, even if we never meet them". Our objective is to develop a customised digital relationship with each customer. This is made possible by what we call "big data". In this environment, "those who win are those who make clear promises to customers and keep them", she concluded.

Although he agreed with Ms CHEVAL on many points, MR KLEIN wished to put two aspects into perspective. "In reality, a small proportion of customers want to do everything themselves. The great majority want to be supported and benefit from the assistance of an adviser. The better-off customers are the most demanding. Private Managers at the banks can testify to this. "Ultimately, although a less expensive model is available, Mr KLEIN is not sure that this aspect is invariably a "decisive" factor. The annual price difference is low and the "low-cost bank provides only a proportion of the services. It does not provide a global service". Basically, it focuses on day-to-day banking needs but does not provide appropriate advice offered by qualified sales staff, according to him. This is a major difference from air travel, for example, where use of low-cost airlines can result in significant savings for the same service, that is getting from A to B. But in banking - although there is certainly a price differential between the models, it is less - and what is more, the service provided is not at all the same", in Mr KLEIN's view. "Make no mistake; there is strong demand for advice and personalised relationships". "And of course, I agree with Marie CHEVAL that for both models you must keep your promises. In a way, it's easier for an online bank than for a traditional bank to keep its promises because customer's expectations are lower" he said.

Will FinTechs and GAFAs "uberise" the banks?

Today, noted Ms Marie CHEVAL, "many technological changes are opening up the field to new players who are not banks", such as FinTechs - frequently start-ups in the financial segment. "There is something worthwhile", she said, the reason why banks are working with FinTechs or even acquiring them, to take advantage of their way of thinking differently, but also for the techniques they use, such as biometrics.

Concerning GAFAs, "these major players must be seen as competitors" but what interests them is not becoming a bank, but achieving added value", she noted, before going on to say: "now players see far more added-value in payment services because they give access to a great deal of data on customers which they can reuse in their marketing or sales programmes". When a customer pays using Apple Pay, for example, there is a transaction with a bank which is no longer visible to the customer. And if a brand is not seen, it is used less, warned Ms CHEVAL. The risk for banks is becoming disintermediated, and that's a worry.

"The challenge is to show banks are capable of providing a user experience which is sufficiently satisfactory to avoid the customer looking elsewhere. It's not only the products, but also the whole customer experience and more". Boursorama is looking into ways of pushing back the traditional frontiers of banks, notably by working on personal finance management. Boursorama has a single secure customer space for all accounts at various establishments: it can categorise expenditure, manage a budget, aggregate invoices and store documents in an electronic safe. The new technologies make it possible to offer these new services. A fundamental aspect since today "innovation in banking is achieved more through services than through products".

Endorsing this point of view, Mr KLEIN emphasised the challenges of payments - “a fundamental subject”. “If we are disintermediated on payments, the quality of data on our customers will be reduced. We must pay attention to that aspect, even if for the moment banks underpin these transactions”.

But they could also be disintermediated “by aggregators”. Capable of connecting all the customer’s bank accounts to the same interface for an overall summary on demand, this service is attracting an increasing number of users (40% of bank customers have an account in at least two banks). And all the more so since the DSP2 directive (Editor’s note: revised directive on Payment Services), which opens up the financial services markets to all - enabling aggregators to become operators.

For the moment, “they have not disintermediated banks which remain the operators and the point at which general relations are conducted with customers”. They remain pure aggregators. But tomorrow, they will have capacity for account-to-account transfers, for example, or even promoting third-party commercial offers. Customers then really won’t need to visit their banking websites, resulting in an increased risk of disintermediation explained Mr KLEIN. However, all this poses significant security risks, since aggregators require personal access codes to obtain bank account information or possibly perform transactions.

The question of what happens next is crucial given potential widespread use of services based on artificial intelligence, so-called “talking robots”, with the aim of automatically offering relevant products to customers since they are based on an analysis of all customer accounts. We might imagine that an aggregator, combined with an artificial intelligence tool with the capacity to send texts and emails to customers on appropriate offers could become an effective replacement for a personal adviser - “it can be envisaged” conceded Mr KLEIN. But banks, like insurance companies, health funds etc. are almost all in the process of acquiring or constructing aggregators. “The excess of aggregators could avoid the outcome we fear”, is his analysis. The answer perhaps lies in the capacity of each bank to have its own aggregator combined with an even more virtuous customer relations model. Because even if we valorise and further enhance the global relationship model, it’s not certain that customers will want more “splitting up” of their banking relations. “Many people are happy to deal with just one or two banks to take advantage of the advice and views of an expert providing global advice”, he considers. In France, “it’s a special relationship which is very strong and in demand. Will it endure? “Enhancing the strong relationship model through a close combination of human and digital is no doubt the key”.

Moreover, FinTech companies will not possess all the capabilities to develop some banking activities entirely under their own steam. Many cooperative relations are in course of formation through the acquisition of some FinTech companies by banks or creation of partnerships for integration of certain aspects of their innovative practices in the banking offer.

How to use big data?

In this evolution, big data will play a decisive role. Tomorrow, a huge quantity of information will be compiled. How can this information be stored while guaranteeing confidentiality and what is the reuse potential? For Ms CHEVAL, in banking, the first challenge for "big data" is to continue guaranteeing the confidentiality of customer data. The new potential data analysis and management techniques open up many applications for enhanced risk management and addressing the right offer to the right customer in the latter's best interest. But before seeking to learn everything about our customers, notably through their social networking behaviour, big data could perhaps be used for "better targeting of customers to send them the right message".

"Sales offers sent by text and email by firms whose recipients are already customers will have an advantage over anonymous messages from a supplier or a platform sending messages of the same type", considers Mr KLEIN. And "the additional call by a qualified adviser will provide significant value precisely because it will be even more customised by construction and supplement the digital prospecting". Now the sales conversion rate at BRED is "considerably higher (ten times higher) when a qualified adviser backs up the digital offer with a telephone call", he confirmed.

More generally, he firmly believes in "bringing together digital models which in their pure form rarely generate profit in the real world and physical models which will not survive for long unless they undergo marked development", taking the example of mass distribution and specialist distribution and Amazon's recent announcement that it envisages creating 400 physical bookshops. "It is in this mix that we will find models pertinent for the future, which certainly will not prevent a proportion of the population only wanting to use online banking, or online banking as a supplement to their physical bank" he concluded. And possibly the appearance of some non-banking players in certain segments of the value chain. There will be several possible models, but "I think, if we approach this correctly, the dominant model will be that of a network bank enhanced by digital technology", provided, however, that initiatives adopted on the priorities referred to are pursued to provide an effective response to the promises made.

How will banks cope with blockchains and Bitcoin

Bitcoin, blockchain … what do the currency and technology really cover and allow? What is the approach of banks? Approaching the blockchain question with "great modesty", Mr KLEIN recalled it first appeared in 2008. "Today, it's said it could eventually have the same influence as the Internet in terms of personal services".

He explained that blockchains are "a huge digital register of transactions, of filed documents, which can be used as trusted third parties. They are managed in a totally decentralised form by thousands of small or large enterprises who have computers holding the encrypted keys which guarantee the integrity of transactions". "Thousands of operators ("miners") permanently participate in rendering the algorithms, verification checks and security of transactions in blockchains ever more complex. The extreme multiplication of the number of players makes it very difficult to imagine that the system could be violated. In any event, this has not yet occurred - although we can't say it will never happen", he continued.

The advantage of the system is that it is an accessible open register for authenticating any document, any exchange between two people, without a third party of trust. Hence, "assets or documents can be transferred, without passing through an external official register and without archivists, in the noble sense of the term, of these registers, and without any regulatory authority". So, there is a "whiff of freedom" hinting in essence that "we can do a number of things without the State", according to Mr KLEIN's analysis. Some people have already filed private marriage contracts. By dispensing with the State, with lawyers, in brief, with systems validated by regulations and the courts, the professions are merged since their main purpose was to authenticate documents. This disintermediation of certain professions may be of interest to banks who could conserve securities - why not on a blockchain at a lower cost? "This use could be considerably extended and cause ruptures in the chain, I am almost convinced of it" he said.

On the other hand, Mr KLEIN is far more sceptical about the use and long-term survival and stability of a currency, for example Bitcoin. "I have a fundamental doubt about the concept of a private currency, whether electronic or otherwise, and the fact that it's in a blockchain changes nothing". "The whole of monetary history, notably since the 19th century, shows that private currencies created by private banks, without a central bank, are exchanged in uncertainty of their relative value, including in a national context, resulting in differential levels of confidence over time, which means that, from time to time, nobody wants one or other currency. So there is no unified value of the currency, of a monetary unit, in national territory", he explained, recalling that "there were very good reasons for creating central banks".

First of all "to unify the value of currencies created by the different banks in a nation. This has an immense advantage: it considerably simplifies trade". The second reason for the creation of central banks is that "previously, the banks regularly triggered financial crises and the failure of banks caused deep recessions which were only slowly overcome and unfortunately, regularly repeated". Central banks, the banks of banks, provide liquidity "at the very time when liquidity is lost by a phenomenon which in reality is a self-fulfilling prophecy. Finally, central banks regulate the banks' creation of money to ensure a nominal anchoring of the value of the currency to avoid inflation or deflation and crises of confidence in the currency". "Hence, I think that the central banks will always be needed to carry out their fundamental roles", he affirmed.

For these reasons, he questioned the future of Bitcoin. "Imagine there is a crisis of confidence about Bitcoin, because there is too much or not enough. Who decides on the issuing of the Bitcoin currency? At such times what would a Bitcoin be worth against the dollar or the euro?" he asked, since "strongly fluctuating values" have already been observed. He considered that "from a theoretical point of view, the currency is totally uncertain, totally without foundation given the historic experience of the last few centuries. Not because Bitcoin is not tied to gold or silver, currencies today are credit currencies but they are based on confidence. Also, Bitcoin's nominal value is not anchored by a central bank and a financial and banking system supervised by a central bank", the lender of last resort.

And finally, if private currency returned, not only would we be confronted by "the worst concerns" as to its value, but also as to its "use". Certainly, the people who create Bitcoin want a clean currency. But how to prevent its use for fraudulent means or for money laundering? In these cases, there is no "authority capable of controlling the monetary flows" noted Mr KLEIN, observing that such an evolution is totally contrary to the trend in recent years worldwide and notably in the developed world".

Are regulations and risk management holding back banking players?

Ms Carole de GAULLE, a compliance expert at the French Banking Federation (FBF), questioned the two participants about a paradox: "regulation is evolving but in the opposite sense to changes in customer behaviour, creating a discrepancy between what is imposed on banking establishments and customer expectations". For Mr Emmanuel du BOULLAY, partner and manager of Associés & Gouvernance, this paradox, combined with "excessive" regulation, "amplifies the burden borne by players who are leaving the banking system and who, ultimately, will compete with banks by leaving them the regulatory part of business".

"The regulators must be very careful to impose the same regulations on all players" emphasised Mr KLEIN. "It is paradoxical for the ECB to conduct an extremely favourable credit policy to avoid deflation and, at the same time, for the same institution to act as a regulator, restricting access to credit by the new ratios imposed" he opined. A "point of equilibrium must be reached". Now securitisation and "non-banks" will in future respond in whole or in part to an excess demand for credit, "which is becoming increasingly commonplace". The problem is "they don't have the same level of regulation" he noted, considering that this was risky from the standpoint of financial stability. "For society overall, it could be contrary to the desired objectives to regulate a sector excessively, so that the normal risks in reconciling the supply and demand for finance, credit, interest rate and liquidity risks, are displaced elsewhere".

On digital technology and security, Maître François FALLETTI, a partner and counsel at the Lyon Bar (Carlara-Lyon law firm), an honorary prosecutor at the Paris Appeal Court, for his part, questioned possible curbs on customers in the form of hacking and effects on privacy. "People's acceptance is evolving rapidly" in this regard, noted Ms CHEVAL, recalling that "a few years ago, many people didn't want to use their bank card number on the Internet, whereas today, it's common practice". But for banks, ensuring the security of systems is an "absolutely key topic which requires ongoing and costly investments", she concluded.