

# BEYOND NORTH STAR GAZING

**How our four winning bank models  
map to actual market evolution**

**WINNING IN THE DIGITAL  
ECONOMY SERIES**



# Preface

New Accenture research attempts to quantify the level of change in the global banking industry structure. We found, for example, that 17 percent of industry players in 2017 entered the industry over the last 13 years. These newcomers have grabbed one-third of revenue growth in Europe, and in markets like the U.K., the combination of high numbers of new entrants and material revenue migration indicates a strong level of disruption already taking place. Incumbent retail and commercial banks must rethink their “North Star” business models and be bold in reorienting their business to be future-ready or run the risk of being left behind as the industry changes around them.

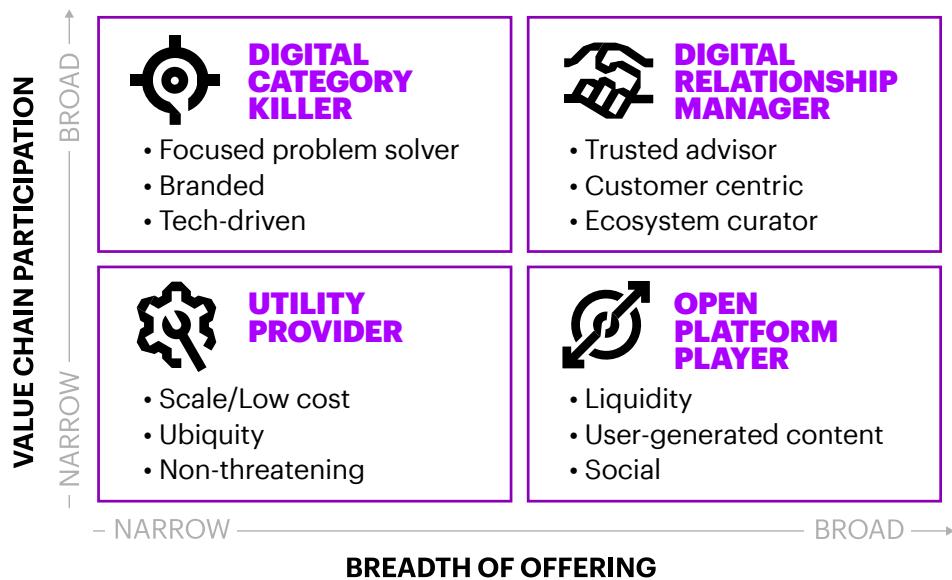
Our research suggests two priorities for incumbent banks; priorities which are addressed in two linked points of view, each of which takes the same industry analysis as its jumping-off point. In **“Beyond North Star Gazing,”** we discuss how the evolution of the industry should shape medium-term business model choices and why not all business models are equally viable in each market. It makes the case that while many banks seem to be defaulting to just being a digital version of their traditional selves, the true strategic challenge is more complex and also more urgent. In the companion report, **“Star Shifting: Rapid Evolution Required,”** we make more of a short-term argument that banks need to take advantage of industry changes to become more relevant to their customers and sustain top-line revenue growth. The advent of Open Banking, digital engagement models and cross-industry platforms all represent threats as well as opportunities for incumbents. To thrive in the future (and earn the right to make the best medium-term strategic decisions), banks need to seize the opportunities to drive organic revenue growth and stay relevant to their customers.

**It's hardly a newsflash that the banking industry is changing. But, by how much and with what impact? Are we witnessing a fundamental shift in industry structure, or does the hyperbole of fintech bloggers and venture capital boosters conceal a stable and enduring banking business model? If banks do need to change, how does individual market structure shape and dictate the relative success of different banking business models?**

Polaris, or the North Star, is perhaps the most famous star in our northern sky, providing a fixed point for generations of navigators. Though it appears reassuringly fixed, Polaris has not always hung directly above the North Pole. Some 5,000 years ago, Thuban in the constellation of Draco was the Pole Star, and 2000 years in the future, scientists predict that celestial navigators (if such a thing still exists) will look to Gamma Cephei for guidance. A star appears to gradually shift in the sky over time in a process physicists call precession, during which the gravitational pull of the moon and sun cause the Earth's pole to point to a different place in the firmament.

In our [Winning in the Digital Economy report](#) last year, we described changing customer needs and the impact of new technology on banking. We also introduced four archetypal business model choices for retail and commercial banks: Digital Relationship Manager, Digital Category Killer, Open Platform Player and Utility Provider (Figure 1). We proposed these business models as north stars that banks could use to guide their strategic decision making. By having clarity of intent, banks could avoid fragmenting both their investments and management focus and circumvent launching a multitude of initiatives while doing nothing particularly well.

## FIGURE 1. FOUR BANKING BUSINESS MODEL CHOICES FOR THE DIGITAL ECONOMY



Source: Accenture

Our intent was that these business models—just like the North Star—would provide stable guidance for banks in the medium term. However, we also recognize that there are precessions at work that could shift the position of these business models over time and also determine each ones' attractiveness in specific banking markets. So, although we advised banks to make a choice and identify their business model North Star, there needs to be constant vigilance to ensure that rapid changes in the local environment don't result in a bank pointing west rather than pointing north without realizing it.

Take new regulation, for example. The effective date for the second Payment Services Directive (PSD2) occurred since our last report, mandating European banks to give third parties access to customer-permitted account and transaction data through application programming interfaces (APIs), and allowing those third parties to initiate payment transactions on behalf of customers. Much of the press coverage has been that PSD2 has been a damp squib, and that nothing has really changed. Yet, we see important strategic initiatives occurring in the market; for example, Deutsche Bank's move to form an alliance with the airline group IATA to cut the card networks out of the payments loop. While still in their infancy, these types of changes have the potential to be very disruptive.

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Similarly, new federal regulation in Australia is requiring banks to make data on credit and debit card, deposit and transaction accounts available to third parties by July 2019.<sup>1</sup> Canada is likely to follow suit, and the Hong Kong Monetary Authority also recently released its draft Open API framework, intended to nurture a better customer experience by changing the competitive dynamics of Hong Kong's banking sector.

Precessions are also acting on the banking industry from the outside, as non-bank experiences teach customers what world-class digital looks and feels like. Accenture consumer research found that 40 percent of global consumers are now potential "Nomads", open to the idea of self-assembling their own suite of banking products from component parts, like a prepaid debt card, a robo-advisor and a personal financial management app, giving a boost to the viability of the platform business model in banking.<sup>2</sup>

Customer evolution is also redefining the interaction model for banks. For example, 66 percent execute half their banking transactions online and 71 percent are open to automated support.<sup>3</sup> More customers are joining online virtual banks (19 percent) than leaving them (8 percent); 31 percent of all customers (and 41 percent of Gen Zers) would consider purchasing banking services from an online provider, such as Google, Apple, Facebook or Amazon.<sup>4</sup> So meeting the competing needs of a fragile, very diverse set of customers is challenging most banks to try and find the proper mix of investments in traditional and digital capabilities.

If you only look at public market valuations, you would conclude that banks are going to find it hard to capture new value or revenue in the digital economy. On average, bank valuations sit at a 1 to 1.5 price-to-book value (with some continental European markets still less than 1), while “bigtech” (such as GAFA and BAT) are valued at 10x multiples and have the majority of their enterprise value predicated on future growth.<sup>5</sup>

With so much change going on in the industry, it’s easy to get fixated on the latest headlines. For example, that Amazon is exploring offering a white-label current account in the U.S. with discounts, rather than interest, as the reward for depositing funds. Or that RBS in the U.K. is shifting to an open platform with its new digital bank set to launch later this year. Rather than be transfixed by the latest shiny object or rumor, we decided to take a step back and try and get beyond the hype to analyze what is really happening to the structure of the banking industry. How many new celestial bodies do we have? How much revenue are new entrants diverting from the traditional banks? Do new entrants conform to the North Star business models we outlined last year? Are traditional banks demonstrating an intent to change, or are they still gazing at the North Stars they have followed for the last few decades?

To answer these questions, we conducted a wide-ranging quantitative study. Specifically, we analyzed structural change and revenue migration in the banking and payment industry, based on banking participation and performance from 2005 to 2017. We analyzed more than 20,000 institutions in the banking and payments market across seven geographies: Australia, Brazil, Canada, China, the European Union, the United Kingdom and the United States to more clearly separate reality from hype.

This report highlights our research findings and discusses the choices banks should make in light of what is actually happening in their markets. There is no single or easy answer, as the mix of business model choices and specific market contexts create a wide range of options. But, what is clear from our research is that an incremental approach by incumbent banks that simply digitally enables business as usual is unlikely to be a winning strategy.

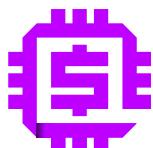
# New arrivals rearrange the banking sky

An overarching conclusion from our research is that the combination of the aftershocks of the global financial crisis, more active regulatory intervention and the emergence of digital-native customers are indeed reshaping the global banking industry. Our research shows that for our in-scope countries, 17 percent of banking and payments players in 2017 are new to the market since 2005 (Figure 2). That is a large number for what had been a very stable industry characterized mostly by internal consolidation. Still, that 17 percent clearly underestimates the level of change in banking. Our 2017 snapshot has a survivor bias, in that the analysis only identifies those members of earlier new entrant cohorts that survived to 2017. For every PayPal, there are scores of fintech payments startups that didn't make it beyond their A-round funding, and hence don't show up in the 2017 numbers.

The new entrants highlighted in our research fall into four broad categories:



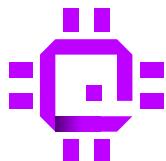
**Challenger banks**, like N26, Atom, Monzo and Starling, that seek to replace a traditional banking relationship with something better. Some started with a banking license, while others launched with prepaid transaction accounts before upgrading to a full banking license. These digital challenger banks emphasize customer experience enabled by technology innovation (AI, Big data, Analytics, Cloud, APIs and so forth). Some, like BMW bank, are subsidiaries of non-financial corporates that have decided that their brand can extend into banking. Others, like Tyme in South Africa, are subsidiaries of existing banks (in Tyme's case, CBA of Australia), seeking to use a new market to try out a new business model.



**Non-bank payment institutions**, beckoned by regulatory changes (most notably PSD2 in Europe) and including e-money institutions and payments processors. These new payments players are often category-killer businesses and have targeted areas as diverse as in-person merchant acquiring (Square), online payments acceptance (Stripe), electronic payments initiation (PayPal) and cross-border money transfer services (TransferWise). Some operate without a payments license (such as Gemalto and Ingenico), while many others hold some sort of payments license, typically with light regulation compared to a traditional bank.

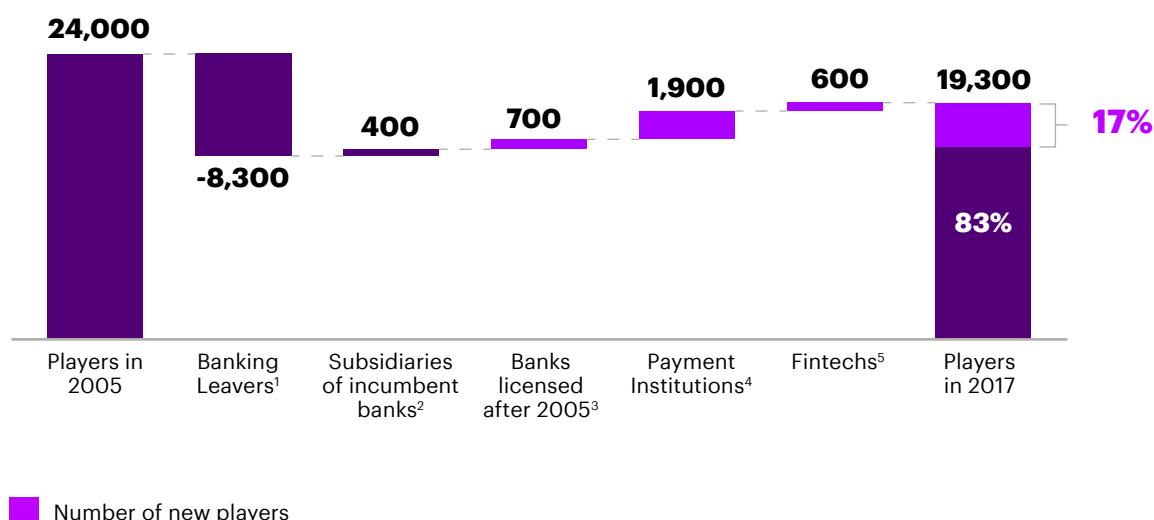


**Credit intermediation platforms** that match borrowers with savers. These span B2C (SoFi) and B2B players (Kabbage, OnDeck) and their funding models range from true peer-to-peer lending to conduits for hedge funds and other institutional money. As intermediaries, they generally operate without a banking license, although as they seek to expand their product offering, many (like SoFi) are considering applying for one or looking to acquire a regulated entity.



**“Bigtech”**—large technology firms, including Google, Apple, Facebook, Amazon, Baidu, Alibaba, Tencent and others—that are encroaching further and further into the banking value chain without becoming insured deposit-taking entities. Their aim is to satisfy the credit, payment and advice needs of millions of customers on their platform while letting traditional banks play the role of stores of value at either end of the transaction value chain.

## FIGURE 2. NEARLY ONE-FIFTH OF PLAYERS IN 2017 ENTERED THE MARKET SINCE 2005



Source: Accenture Research Analysis on Central Banks, payment registries and CB Insight data

Countries in scope are: US, UK, Europe (EU), Canada, Brazil, China (excluded Shadow Banking) and Australia

1. Divested, ceased or impacted by M&A

2. Either with banking or payment license

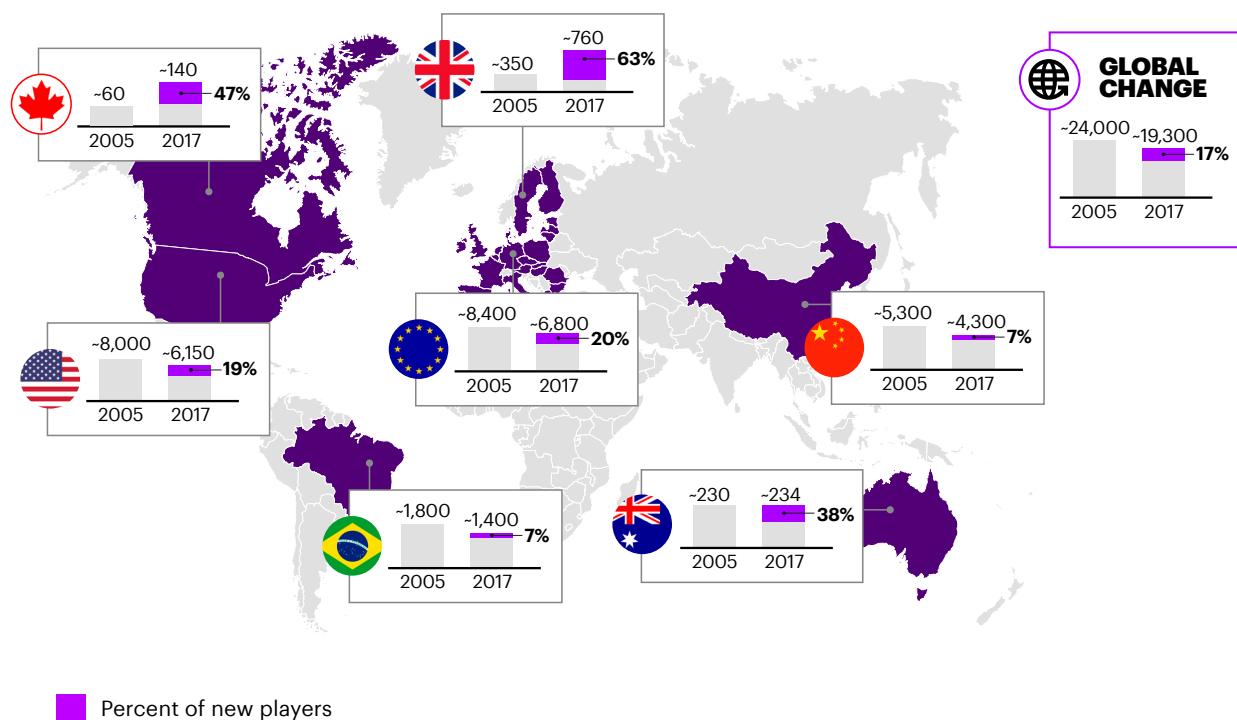
3. Players to whom was granted a banking license after 2005

4. Institutions licensed as Payment System Provider and/or E-money Institutions that do not hold a full banking license, plus relevant processing players even if without payment license

5. Fintech start-ups offering banking services, b2b and b2c, with mid or later stages of financing round

While structural change in banking is a global phenomenon, its magnitude varies by country (Figure 3). The percent of new players is highest in the U.K. (63 percent), where new regulations, backed by the Financial Conduct Authority and the Competition and Markets Authority, have explicitly sought to increase banking competition and reduce the dominance of the established banks. Some 15 fintechs in the U.K. have now received a banking license, and the leading challenger banks are now breaching the one million customer threshold.

### FIGURE 3. THE MAGNITUDE OF INDUSTRY STRUCTURE CHANGE VARIES BY COUNTRY



Source: Accenture Research Analysis

When faced with these numbers, traditional bankers tend to offer three rationalizations that allow them to dismiss new entrant activity as unimportant and, instead, stay focused on their long-established North Star. The first rationalization is that many of these new entrants are simply putting an elegant user interface on traditional banking products and that, with the right design talent, incumbent banks can be competitive. To an extent this is true. In the U.S., the most meaningful change in the current account market has been the recent dominance of the “big three” (Bank of America, Wells Fargo and Chase) in gathering over 50 percent of new accounts based on their multi-billion-dollar investments in digital customer experience. Among U.K. banks, Barclays’ mobile banking app was ranked highest in Forrester’s recent mobile app report<sup>6</sup> and also in Forbes “Great British Mobile Banking Review” for both 2017 and 2016,<sup>7</sup> ahead of a raft of new challenger banks

However, there is also plenty of true business model and solution innovation happening among newcomers. Consider Transferwise’s retail foreign exchange solution that matches people in different countries who have a reciprocal need to change money into another currency and, hence, avoids the actual conversion of the currency through traditional FX trading.<sup>8</sup>

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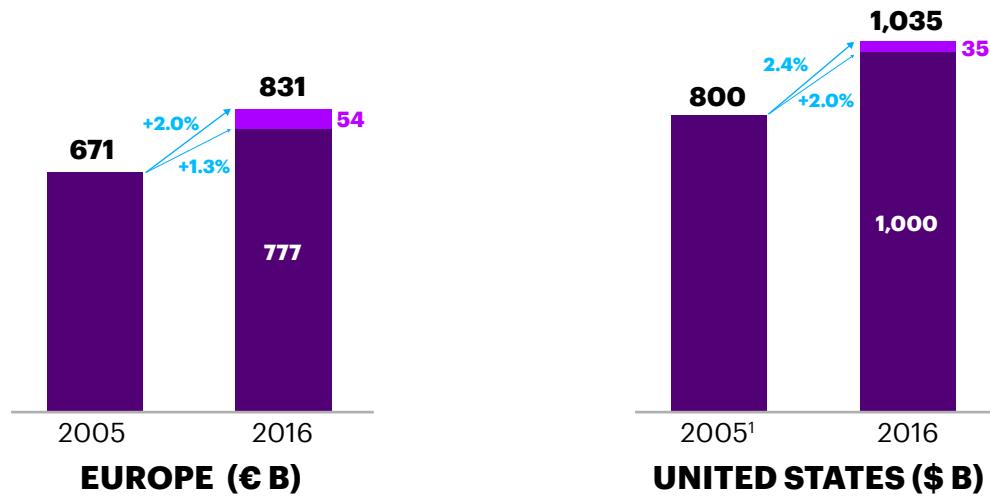
Alternative lenders, like Upstart, Avanta and SoFi are taking credit underwriting and pricing beyond traditional FICO-driven scorecards to incorporate full-spectrum underwriting that better discriminates the likelihood of default.<sup>9</sup> Finally, Germany’s Fidor Bank is offering its Open Banking platform-as-a-service to allow others within its ecosystem to create financial services marketplaces under their own brand, bringing “what’s best in the market to customers.”<sup>10</sup>

So, while there is plenty of skin-deep design hype in the world of new banking entrants, there are also many other examples of true innovation happening around the world that can’t be dismissed so easily by incumbents.

# Now, revenue is starting to shift

The second rationalization offered by incumbents for continuing to gaze at their traditional North Star is that despite all this new entrant activity, no real revenue is actually moving. Again, there is a grain of truth to that statement. It's true that the percent of revenue migration to new entrants is lower than their share of institutions. For example, in the U.K., although 63 percent of institutions are new, they have only taken around 14 percent of revenue. However, this is a classic stock-versus-flow situation where the focus of incumbents should be firmly on the flow as the leading indicator of medium-term changes in stock. Our analysis suggests that new entrants have captured six to seven percent of revenues in Europe and three to four percent in the U.S., seizing a full one-third of new revenue creation in Europe (Figure 4) .

**FIGURE 4. BANKING AND PAYMENTS REVENUE IN U.S. AND EUROPE**



Source: Accenture Research analysis on ECB and S&P Capital IQ data

1. Data includes Banking and Payment players

█ New players

█ Incumbent players

% = CAGR

The numbers are even more dramatic when you look at China, where Alipay and WeChat together have more than 1.3 billion mobile payment users and account for 94 percent of that market.<sup>11</sup> In Japan, Rakuten, the e-commerce giant, is now the largest online bank, with some six million customer accounts, although its balance sheet remains a fraction of the size of the incumbent banks. In the U.S., traditional commercial bank balance sheets in 2017 were irrelevant, accounting in aggregate for only three percent of new corporate credit extended, while the rest was accounted for by either the capital markets or direct credit investments by institutional money—much of which was intermediated by new credit platform players.<sup>12</sup> Loup Ventures estimates that there are now more than 125 million global active Apple Pay users, representing 200 percent year-over-year growth, and 16 percent of the active iPhone base.<sup>13</sup> Finally, according to Starbucks, its payment app was used for more than a third of its retail payments and had more active users in the U.S. than Apple Pay.<sup>14</sup> And just to be clear, Starbucks' success metric is not payments revenue; instead, they have a laser focus on store-level revenue growth enabled by a better customer experience, of which invisible payments is only one component.

Another interesting conclusion from our research is that revenue migration is not directly correlated with new entrant activity. Those investors that thought they could disrupt the Canadian banking industry have funded a lot of new entrants; yet, their impact has been negligible, representing less than two percent of total banking and payments revenue. As we will discuss later in this report, the relative stability of Canada's banking sector and the conservative nature of its customer base has created rocky ground in which fintech seedlings are trying to grow. Compare that to the U.K., where the combination of customer dissatisfaction and regulatory intervention has resulted in well-tilled, fertile soil.

The third major reason incumbents use to discount the impact of new entrants is that, even if revenue is migrating, the new entrants aren't making a profit. That is certainly true when we look at the superstars of the European new entrant class over the last three years where the data shows that the only ones making money are those with a traditional bank balance sheet (Figure 5).

## FIGURE 5. PROFIT PROFILE OF 18 HIGH-GROWTH NEW ENTRANTS IN EUROPE

18 EUROPEAN NEW ENTRANT WINNERS	2014-2016 REVENUE COMPOUND ANNUAL GROWTH RATE	2016 PROFIT MARGIN
Bank License	<b>164%</b>	<b>14%</b>
Payments License	<b>139%</b>	<b>-5%</b>
Unlicensed Fintech	<b>187%</b>	<b>-31%</b>
Weighted Average	<b>156%</b>	<b>8%</b>

Source: Accenture analysis on S&P Capital IQ Data and Annual Reports

But the fact that new entrants aren't making money should be scant consolation for any student of the broader digital economy. A key lesson from the last decade is that if you are capturing ground and establishing strategic control of the customer, then investors are willing to stomach many years of losses. For firms caught up in the U.S.'s retail apocalypse, like Sears and JCPenney, it doesn't help much to point out that Amazon hasn't made much profit for most of its existence. What is clear from the digital transformation of retail, entertainment and the media is that the spoils of digital disruption are not evenly distributed, and once market dominance is established, sustained losses can turn into gargantuan profits relatively quickly.

# Are our four winning business models new North Stars for banks?

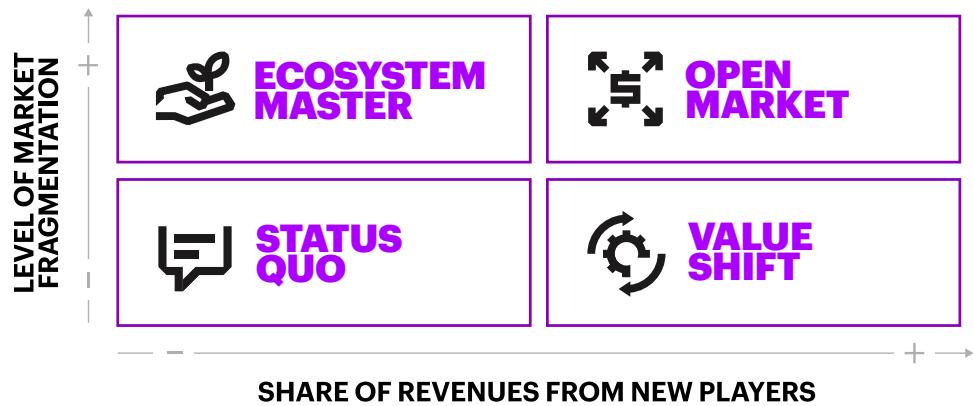
In bank boardrooms around the world, there is a growing recognition that these three rationalizations for dismissing new players don't hold water, and that industry change—potentially of the existential variety—is now at hand.

Consider that in the U.S., these should be the best of times. Unemployment is around four percent, GDP growth is strong, and interest rates are rising. Yet, many regional banks are struggling to grow their balance sheets, and much of their focus is still on cost reduction and internal industry consolidation rather than net new customer growth. In more stable markets, like Australia and Canada, banks are building new ecosystems of partners and attempting to ensure both future relevance and vitality before their revenue and profitability start to leak out to new competitors.

In last year's **Winning in the Digital Economy report**, we advocated that banks be clear about the business model they were adopting and commit to it 100 percent. We introduced four archetypal business models we believe to be viable choices for retail and commercial banks as they compete in the digital economy (see "Four Banking Archetypes that Can Succeed in a Digital World"). What we have learned from this second phase of research is that market context matters tremendously when making that choice.

As described earlier, the principal dimensions for measuring market disruption are the level of market fragmentation due to new entrants and the level of revenue migration (with the assumption that profitability will follow over time, if investors have the patience and management skill to monetize a strong market position). Through this lens we can categorize the world's banking markets into four main quadrants (Figure 6) within which banks can consider their best-fit business model choice.

## FIGURE 6. FOUR MAIN TYPES OF BANKING MARKET



It is dangerous to believe that any market, except those that are heavily regulated, will remain in the Status Quo quadrant for long. The closest in our analysis may be Brazil, where incumbents continue to enjoy a combination of high market share and high returns. However, the Nomad customer group in Brazil is over 60 percent, indicating a desire for alternatives. Also, the Brazilian banking regulator is now considering an Open Banking approach that may create plenty of room for new competitors. Given the relative stability of the market, Brazilian banks do have an opportunity to become a better version of themselves and focus on adopting the Digital Relationship Manager model that will allow them to continue to be most things to most people. But almost inevitably, we will see the emergence of Digital Category Killers in Brazil, looking to disrupt the industry by doing one thing very well. Some of those may be global in nature, for example, if PayPal were to make a play. Or, it could be an established bank from another geography entering the local market with a focused proposition. Without fragmentation, the Status Quo market is unattractive to both the Open Platform Player and Utility Provider models, as there is simply not enough of an ecosystem of fintechs and new offerings to power or aggregate.

While there are plenty of new entrants in Ecosystem Master markets, like Canada and Australia, their revenue impact has been limited. In these markets, incumbent banks tend to focus on the Digital Relationship Manager model and, given the lack of traction of new entrants, can look to extend their ecosystem reach into non-financial activities to create a better customer experience and a more defensible perimeter. Recent moves by Royal Bank of Canada to create a small business support business<sup>15</sup> and a digital hub for car ownership<sup>16</sup> are just two examples of how incumbent banks can build on customer goodwill to create a broader and deeper business model from a Digital Relationship Manager foundation.

# Four banking archetypes that can succeed in a digital world

Based on Accenture's market analysis and financial services industry experience, we believe there are four archetypal business models that can be successful in the digital retail and commercial banking market of the future:



**Digital Relationship Manager**, a vertically-integrated model with a focus on sustaining the unified balance sheet. It draws on banks' strengths of established customer relationships, data access and trust to differentiate the entire banking offering. In an environment where many new players are trying to nibble away at existing revenue streams, Digital Relationship Managers can extend their business model to capture more of their customers' wallets and embed themselves in more transactions.



**Digital Category Killer**, a model that serves a narrow set of customer needs with best-in-class branded products and services while keeping its own value chain participation high. The best become ubiquitous and build a best-in-class brand that people value and competitors are unable to duplicate. For incumbent banks, building new Category Killers may be a way to become more open quickly. They can then look to migrate the rest of the bank to that model over time or build a linked portfolio of those offerings that begins to replicate a traditional comprehensive banking offering.



**Open Platform Player**, a model that masters a customer-centered platform through which other product providers (most likely Digital Category Killers and Utility Providers) can interact with customers and create and sell differentiated and value-added products and services. These platforms allow customers to assemble a complete best-in-breed financial services product suite by partnering with specialists in each area and providing the aggregation, integration and social layer that sits on top.



**Utility Provider**, a model that narrows the bank's customer focus and value chain participation to offer complete product solutions to players who manage the end customer relationship, or to simply provide a regulated balance sheet to which third parties can book assets and liabilities. Utility Providers can maximize their reach by working behind the scenes with a focus on being easy to work with and simple to connect to. In a more fragmented market, there will be more partners looking to draw on third-party capabilities. Being the scale, low-cost provider of these services could be an attractive growth strategy, particularly for those with the appetite to grow their balance sheets.

The best example of a Value Shift market is China, where bigtechs like Ant Financial and Tencent have made serious inroads into the consumer financial services market and traditional banks are clearly in catch-up mode. Attempting to be a Digital Category Killer in this market is dangerous, as Ant Financial has shown that its customer relationships allow it to launch and scale new products at speed (Figure 7). Also, with many people in China running their lives through WeChat, any effort to create a financial services-specific platform business looks doomed to fail. As consumer product manufacturers in the U.S. learned, ceding the customer relationship to big-box and bigtech retailers, like Walmart and Amazon, means that the only real choice is to become a product supplier. In China, this could suggest that banks embrace one of two approaches: become a Utility Provider that sits behind the BAT and other dominate channel players (hoping that they don't build their own) or try and build Digital Category Killers that have enough prominence to force a partnership with these dominant channels.

## FIGURE 7. THE LARGE AND GROWING ANT FINANCIAL UNIVERSE



Source: Accenture Research Analysis

1. [Technode](#)
2. [The Wall Street Journal](#)
3. [Business Insider](#)
4. [The Telegraph](#)
5. [Bloomberg](#)
6. [Eonow](#)

One could argue that of all of the markets we examined, the U.K. is the best example of the Open Market quadrant, in that it has material fragmentation and real revenue migration. U.K. banks can play defense and try to be a Digital Relationship Manager, but recent decisions by both HSBC and RBS to experiment with open platform models and the decision of some Digital Category Killers, like Starling, to also open their platforms to third-party apps suggest that the U.K. may be the first market in which marketplace banking becomes a truly viable business model. With high levels of fragmentation, the Utility Provider play can also become attractive as evidenced by new players, like ClearBank, that only exist to serve the needs of new customer-facing players. Yet fragmentation also creates opportunities for more traditional banks, like Bank of Ireland (which powers both the Automobile Association and Post Office banking offerings), to focus on enabling channel partners in the U.K. with product capabilities and a balance sheet.

So, what of the rest of Europe and the U.S.? These markets probably offer the most strategic optionality, because they sit somewhere at the point where all four quadrants converge. Thus, all four of the winning business models are possible, although regional and community banks in the U.S. have less degrees of freedom and may be forced into either trying to compete with the majors as Digital Relationship Managers or renting their balance sheets under a Utility Provider model.



# Incumbents still gravitate to the Digital Relationship Manager model

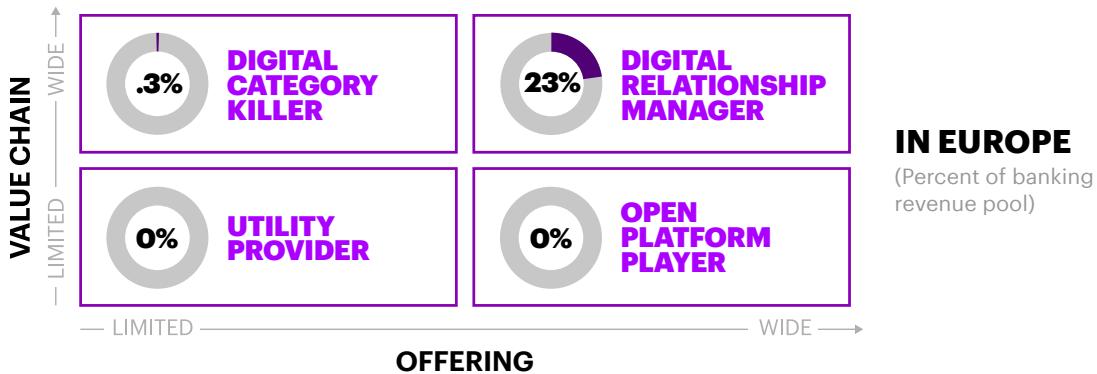
We have shown that picking the right North Star is a market-specific decision. So, from market to market, we would expect incumbent banks to make a range of business model choices to maximize their chances of success.

That's the theory. But, what does the data actually show? Based on our analysis, it points to three truths for incumbent banks:

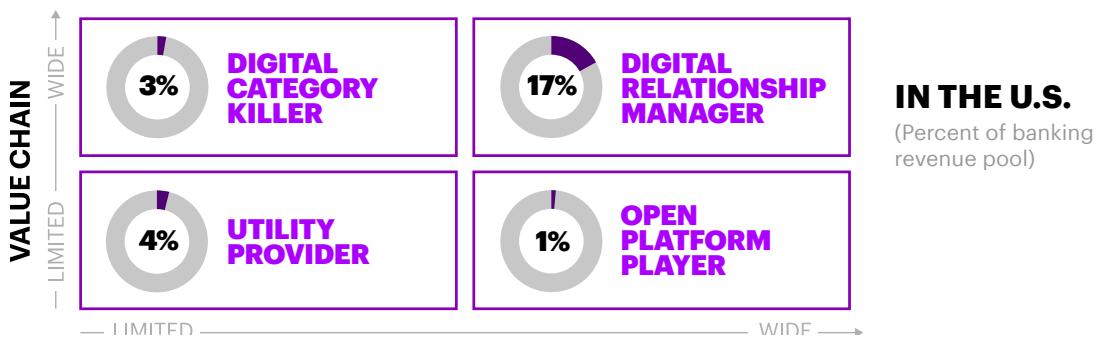
- **01.** Only a minority are making clear strategic choices.
- **02.** Of those, most are defaulting to the Digital Relationship Manager model.
- **03.** Choosing the Digital Relationship Manager looks like the safe, incremental choice, but executing it well represents a huge revolutionary change for most incumbents.

Incumbents that were able to rotate to a new business model represent less than 25% of revenues in Europe. The vast majority have chosen the Digital Relationship Manager model which allows them to continue to offer a broad set of products and services to a wide range of customer and partner segments. In the U.S., we estimate that around 25 percent of the current revenue pool has made a choice about how to compete, with a little more diversity of models, although the Digital Relationship Manager is still the dominant choice (Figure 8).

## FIGURE 8. INCUMBENT BANKS IN EUROPE AND U.S. GRAVITATE TO DIGITAL RELATIONSHIP MANAGER IN ROTATION TO THE FOUR ARCHETYPE MODELS



Note: Analysis based on top 100 European incumbent banks located in 15 European countries



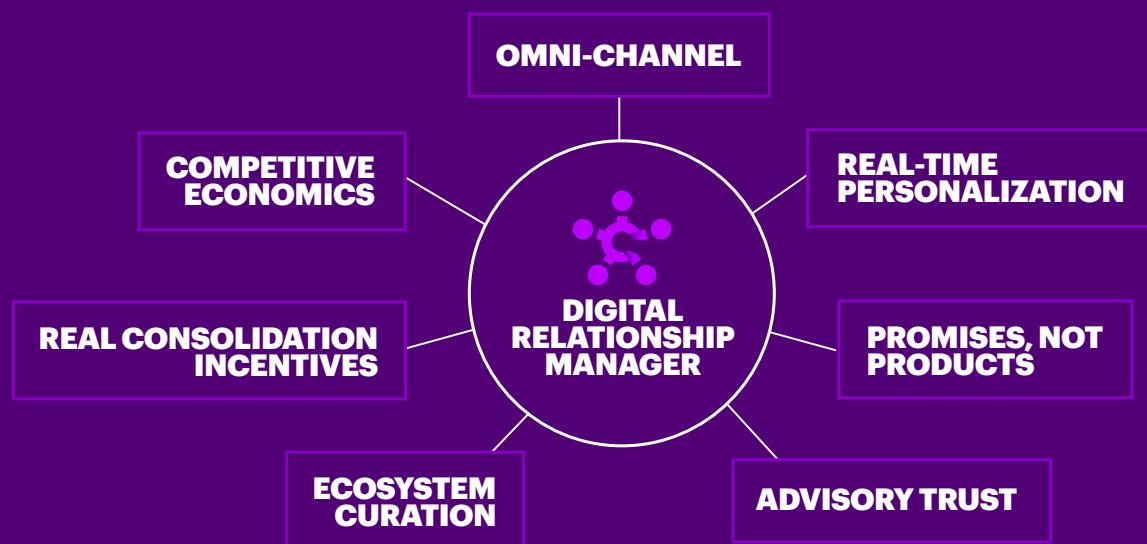
There are many good examples of positive choices by banks to adopt a Digital Relationship Manager model. Danske Bank in Denmark offers Sunday, a digital tool that broadens their participation in the house buying journey. The tool, serves both as a personal housing loan calculator and a filter site that shows homes that a house hunter can afford and how a specific home purchase will affect their financial situation.<sup>17</sup> Similarly in Canada, RBC® offers a six-step digital Home Buying Readiness Quiz to help consumers see if they're ready to be a first-time home buyer with tips on neighborhood selection, home valuation and affordability to help customers reach their goal of home ownership.<sup>18</sup> In the U.S., the focus has been less on ecosystem plays and more on integrating across traditional product silos to provide better advice—often via virtual assistants, like Bank of America's Erica.

# The distance of the Digital Relationship Manager North Star

The incumbent bank shift to a Digital Relationship Manager is tough to do and this North Star is light years away for most banks. Even with the advances the industry has made towards digital banking, the transformation still requires radical change.

For banks to rotate to a competitive Digital Relationship Manager model (Figure 9) means enabling a seamless flow of information across channels, personalization of offers and wallet consolidation incentives through relationship pricing. Artificial intelligence can help in breaking down traditional product silos and making banking very simple, intuitive and personalized for customers. Given the complexity, banks may need to position their role as a Digital Relationship Manager along vertical lines, specializing in a specific customer segment (such as an industry group in commercial or a job category in consumer) to narrow their transformation focus. Modern, technology-based strategies, like **digital decoupling**, will help banks free themselves from their legacy system constraints and give them the flexibility to shift from a product- to a customer-centric organization.

**FIGURE 9. WHAT GOOD LOOKS LIKE IN DIGITAL RELATIONSHIP MANAGER BANKING**

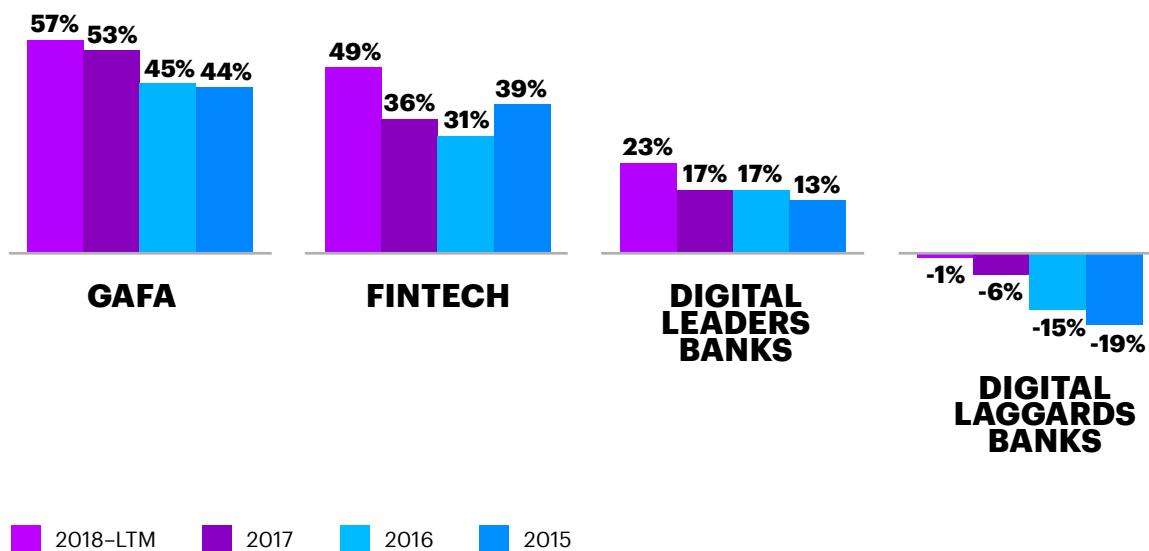


Despite such notable innovations and the distinguished company on the path to the Digital Relationship Manager, the harsh reality is that many banks striving to rotate to this model are likely to fail. Without an optimized traditional model that provides plenty of fuel for growth, many banks will not have the investment capacity to stay competitive as a Digital Relationship Manager. We see that happening with digital laggard banks, and their future growth value reflects it: a negative one percent compared to digital-leader banks at 23 percent (Figure 10).

## FIGURE 10. VALUATIONS INDICATE CHALLENGES FOR DIGITAL LAGGARD BANKS

### Future Growth Value Analysis

(% of Enterprise Value, Jun 2018)



Source: Accenture Research analysis on Capital IQ data as of 5th Jun 2018, d and Citi data

Notes:

LTM = Last Twelve Month (sum of Q1'18, Q4'17, Q3'17 and Q2'17 financial numbers)

Enterprise value is the average value for respective years from 2015 to Jun 2018.

Fintech 40 companies, Digital Leaders 22 banks, Digital Laggards 51 banks, Future Value = enterprise value less value of current operations.

Analysis based on average market cap over the year.

# New entrants are being pulled towards the other three business models

As we're already seeing, new entrants are opting for choices other than Digital Relationship Manager due to their digital-only nature, freedom from legacy structures, and narrow focus.

## OPEN PLATFORM PLAYER

Open Platform Players can serve as pseudo-Digital Relationship Managers through outstanding orchestration. They are primarily fintechs and digital banking startups (or challenger banks) focused on building and surrounding one core product (such as a current account or payment account) with the power of a modern digital platform, fueled by broad API-based offerings that allow easy import and export of services with other third-party players. Good examples are Monzo, Starling and others in the U.K.—home to the world's most advanced digital challenger bank ecosystem due to an outsider-friendly regulatory environment. Belgium-based fintech banqUP is a good non-U.K. example. It offers a one-stop-shop marketplace where SMEs can access services to address business needs (like accounting, financial and budgeting).<sup>19</sup> Without the burden of legacy systems, Open Platform Players generally offer fast, efficient and low-to-no fee services at competitive rates atop a compelling, always-on digital customer experience.

Though embraced predominantly by newcomers, incumbents are also exploring this model as a way to become open while also remaining keeper of the customer relationship and trust. Spain's BBVA, for example, pioneered this model when it launched the BBVA API Market. The solution makes commercially available ten of the bank's APIs to outsiders and positions BBVA to "become the best platform" on which to build new digital experiences.<sup>20</sup> RBS, Citi, Santander, Barclays, Capital One, DBS Bank and other big banks now make APIs open and available to third-party developers.

And, the market for Open Platform Players is expanding. Australia just licensed its first digital challenger bank<sup>21</sup> and Europe's N26 is expected to launch in the U.S. later this year<sup>22</sup>—which will likely lead to unbundling of services in these markets. Further strengthening the viability of the Open Platform Player model is banking services

delivered as part of a platform positioned at the broader financial services or cross-industry level. That is both the attraction and the threat of Amazon Banking, where a fully functional current account provided on a white-label basis by a traditional bank becomes the transaction enablement vehicle for all of your online (and ultimately offline) commerce.

## DIGITAL CATEGORY KILLER

Though the majority of new players in Europe are Digital Category Killers, they represent less than one percent of the revenue pool, according to our analysis. They focus on one or a few specific products and deliver them through an innovative customer experience. This is the case with Transferwise and WorldRemit in money transfers, and Iwoca and Kreditech in consumer and small business lending. In the U.S., three percent of banking revenue now goes to Digital Category Killers—the likes of PayPal®, Venmo, Rocket Mortgage®, Betterment and others.

Marcus by Goldman Sachs®, launched in the U.S. in 2016, is a good Digital Category Killer story from an established financial services player. It is an online platform offering no-fee personal loans and high-yield savings accounts to consumers. At the end of 2017, Marcus had more than \$2.3 billion in loans, \$17 billion in deposits and more than 1.5 million customers.<sup>23</sup> Recent acquisitions of virtual card and personal financial management startups also suggest that, over time, it will migrate to the Digital Relationship Manager quadrant, offering a broader array of personal financial services products.

## UTILITY PROVIDER

Both in Europe and in the U.S., this model is limited to few cases. These include Cross River Bank which offers banking-as-a-platform services that let other companies quickly and easily offer banking products to their customers with strong operational efficiencies and compliance oversight. In 2015, Cross River helped originate more than \$2.4 billion in loans for fintechs like Affirm and Upstart.<sup>24</sup> Cross River set a new monthly loan origination record of more than \$600 million in April 2018, representing some 60 percent growth in loan origination from April 2017 and working to keep the bank on pace to exceed \$7 billion in loan originations for 2018.<sup>25</sup>

SolarisBank in Europe also acts as a Utility Provider, offering various modern banking APIs that include account and transaction services, compliance and trust solutions, working capital financing and so forth. Others in Europe aligned to this model include ClearBank (U.K. payments clearing) and Fidor (through its banking-as-a-service solution).

# Celestial navigation: a critical time for banks to go beyond simply gazing at the new North Stars

The traditional static North Star of the banking industry appears to be moving and, in some markets, the precession is happening quickly. To compete and stay relevant, incumbents need to respond with both clarity of business model and speed of execution to align to a new North Star. Primarily, this comes down to banks doing five things:

**01.** **Understand the nature of their own market** in terms of fragmentation and revenue migration and use that knowledge to establish which business models will be successful in that market and where competition is likely to come from. Our research suggests that doing nothing and relying just on the incremental evolution of the traditional business model is not tenable, given the pace of change we are seeing around the world.

**02.** **Having chosen a new North Star, stop doing things that don't align with that business model** and are management distractions that sap scarce capital expenditure and non-interest expense. If the bank is running a portfolio of business models (with potentially different choices in expansion versus home markets), then ensure cross-pollination of ideas, innovations and enabling technologies without blurring the lines between the business models themselves.

**03.** **Given the business model choice, be crystal clear about where incremental revenue growth will come from through that model.** Will the bank take wallet share from existing customers, acquire new customers into that model, or serve other firms that will own the ultimate customer relationship? Future value will require strong organic revenue growth which is likely to be a zero-sum game in most markets. In the stock-versus-flow dynamic described earlier, the pace of new customer acquisition or wallet share capture is a critical leading metric that can't be ignored. Banks need to be relevant now to customers rather than resting on their laurels and assuming customer inertia.

## 04.

**Create a technology and operating model aligned to the destination business model.** In all four archetypes, the challenge is not to be constrained by legacy technology architecture but instead create a digitally-decoupled approach that is capable of competing with the best of the new entrants and moving at their speed. New entrants (both fintech and bigtech) are truly agile, built on cloud platforms and capable of reinventing themselves on a cycle time that is far quicker than most incumbent banks. Markets like China are evidence of how quickly customers can migrate when there is clear blue water between the offerings of new entrants and incumbents, so incumbents in other markets can't afford to let that type of gap emerge.

## 05.

**Understand the essence of what the bank is as an institution and shape a business model that takes advantage of cultural strengths.** If the bank is positioned as efficient, buttoned-down and low-risk, then perhaps letting another brand manage the customer relationship while the bank delivers a world-class back office is the right strategy. The biggest danger for most incumbent banks in the next decade will be identifying too strongly with their existing North Star and not realizing that it is possible to realign the institution and use its current assets, strengths and capabilities to point in a different direction and be successful.

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**The stars have aligned: new entrants are here, material revenue is beginning to shift, and it is all beginning to happen at increasing speed. Banks must act before it is too late, rotating quickly to their new model to compete in a fragmented, highly competitive and open landscape.**

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## RESEARCH METHODOLOGY

Accenture Research analyzed more than 20,000 institutions in the banking and payments market across seven geographies: Australia, Brazil, Canada, China, the European Union, the United Kingdom, and the United States. We relied on data provided by the European Central Bank (ECB), local central banks, and various financial supervisors. We excluded statistically irrelevant smaller companies, mostly in the payments area. Of the companies analyzed, 3,200 were considered new players (having entered the market since 2005). New institutions fall into three main categories: licensed banks, payments players (payment system providers, including e-money services, and payment system operators other than banks), and non-licensed new players in banking and payments, including well-established "fintech" start-ups (receiving mid- to late-stage funding in the past five years). For selected markets (Canada, the European Union, the United Kingdom, and the United States), we conducted an additional bottom-up analysis of the banking and payment revenues captured by new players vs. incumbents. The analysis was based on company data, where consistently available, and on an econometric model to estimate the unreported revenues.

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