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# ***FinTech 2.0***

Beyond blurred lines: Have Financial Services Institutions misread the innovation landscape?

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# Executive summary

*In five years, we won't be talking about FinTech anymore.*

*Now I realise that's a strange way to start the first ever PwC New Zealand FinTech Survey, but it's true. The distinctions we're now seeing between FinTech start-ups and today's incumbents could well disappear completely as corporates harness their own transformational potential and today's start-ups mature.*

Last year, our Global FinTech Survey was titled “Blurred Lines” – referring to the growing ties between FinTechs and corporates. Now, with FinTech 2.0, we're looking forward to a world of no lines. At this point we have to ask; will today's start-ups have the size and market share to be the new incumbents? And how will today's banks, insurers and asset management companies undergo their own transformation? These changes will be profound, and these new hybrid Financial Services will look nothing like today's companies.

This presents a clear challenge to New Zealand corporates: the FinTech revolution won't just be driven by start-ups. It will come from the established competitors you thought you knew, but are already a step ahead in the race to a hybrid model.

Our New Zealand participants don't seem to have grasped this yet – they're still heavily focused on FinTech start-ups. All of our respondents said start-ups will disrupt Financial Services, while 86 per cent said it will come from internet platforms and social media, both well ahead of the global results. Where today's corporates aren't focusing is on their existing competitors – our global respondents were twice as likely to predict disruption coming from existing Financial Services institutions as our New Zealand survey participants.

For established businesses, these changes in the Financial Services sector are demanding a root-and-branch rethink of the way we run a Financial Services company. FinTechs can provide some clues, but they're on their own transformation journey. Established companies that underestimate their own potential, and that of their competitors, do so at their own peril. Those that look beyond the start-up hype and can develop a two-speed innovation strategy (see page 21) will be successful in the long-term.

I'd like to thank all of this year's survey participants who have helped us to bring the FinTech Survey to New Zealand. It's an exciting time to be in Financial Services and I hope this year's report helps spark the right kind of change in your organisation.

**Andy Symons**

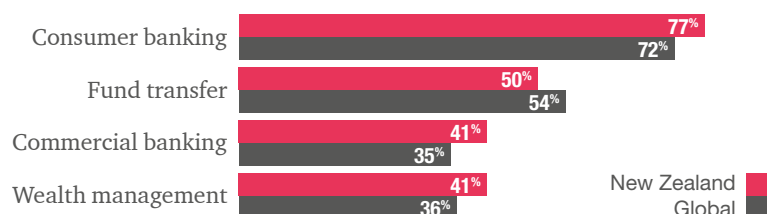
Financial Services Sector Leader and Innovation Partner



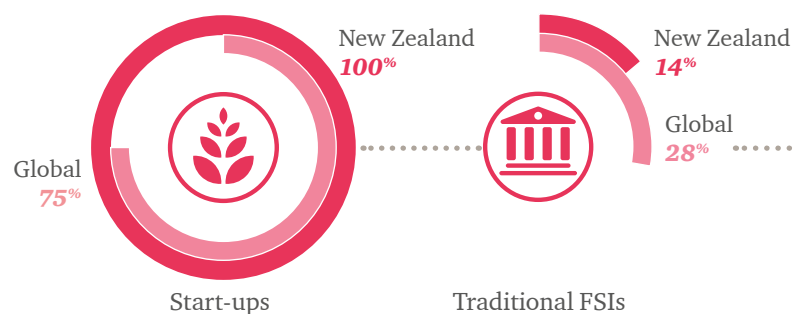
## Seeing the bigger picture on FinTech

Wondering how the FinTech revolution is shaping Financial Services? Here are the key findings from our first New Zealand report.

Q: Which parts of the financial sector are likely to be the most disrupted by FinTech over the next 5 years?



Q: Which entities are likely to be the most disruptive in the next 5 years?

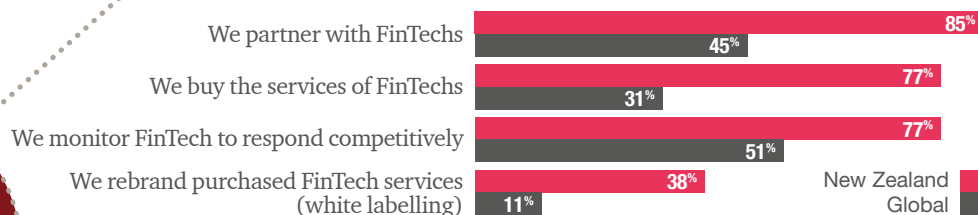


Of current customer interactions are handled through a website

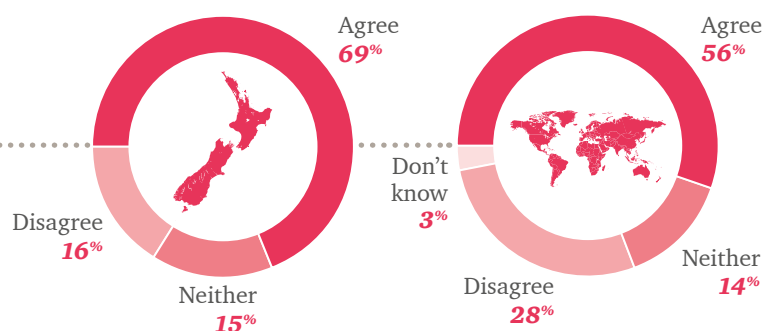
57%



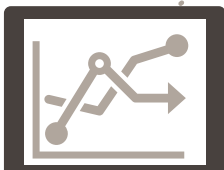
Q: How are you currently dealing with FinTech companies?



Q: Has your organisation put disruption at the heart of its strategy?



 **35%** *interact with customers through an app*, compared to 28% internationally

 **Data and analytics** and **mobile** are the most popular investments for the next 12 months (77% and 55% respectively)

## The Future of FinTech

### Where are the blind spots for today's financial institutions?

It's easy to assume that the FinTech revolution will be driven by FinTech start-ups and internet companies. We've already seen these companies winning over customers and investors with new services, easy-to-use products and a customer-centric approach that has left corporates scrambling to catch up.

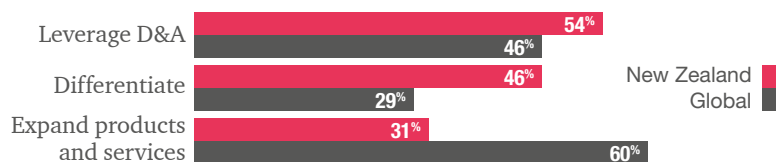
Against that backdrop, it's no surprise that these companies ranked highly as a source of disruption. All of our respondents thought that the most disruptive force in Financial Services in the next five years would be start-ups, while another 86 per cent pointed to internet companies. That compares to global averages of just 75 and 55 per cent respectively.

The danger we saw in our survey data is that this focus on start-ups is coming at the expense of other potential sources of disruption. Local respondents were half as likely to see traditional corporates as a source of disruption (28 per cent internationally vs 14 per cent in New Zealand). Compared to our global findings, local companies are overestimating the impact of start-ups, and underestimating the disruptive potential of themselves and their competitors.

When we drill down to the details of this engagement, the picture becomes clearer. Almost all (85 per cent) of our respondents said they are entering into partnerships with FinTech start-ups. However, the risk that comes with these partnerships is that established businesses treat a FinTech partnership as a chance to outsource innovation to a start-up, rather than a starting point for a much wider transformation in their operations.

#### The broadening FinTech horizon

Q: Which of the following do you want to strengthen to capitalise on new opportunities?



## FinTech: What is it good for?

Established Financial Services companies are looking to use FinTech as a point of differentiation – something that's far more common here in New Zealand than it is overseas. Almost half (46 per cent) of our local respondents said differentiation is a key benefit from FinTech, compared to just 29 per cent internationally. In New Zealand, only leveraging existing data and analytics was seen as a more popular opportunity that FinTech is creating.

It's hard to underestimate how important differentiation will be for established Financial Services. The biggest force for change in the next five years won't be a start-up, but an existing firm that has redefined itself with a clear, articulate and compelling point of difference in the market. That point of difference will certainly be supported by the latest technology, but it will represent a more fundamental change in the product offering and market presence of today's established Financial Services companies.

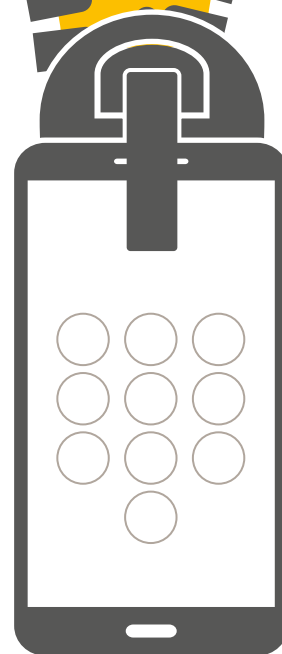


*The gap between FinTechs and Financial Services institutions is closing fast, but incumbents are struggling to translate this into a coherent innovation strategy.*

*While all our respondents see start-ups as a source of disruption, only*

**14%**

*think existing institutions have the same potential.*



## Customer centricity and service simplicity

### What will drive the next generation of financial products and services?

You can't understand the huge changes in Financial Services by solely looking at the dynamics of FinTech start-ups. These companies have certainly made their mark, but in many cases they are simply capitalising on the underlying dynamic of changing customer preferences.

In New Zealand, companies are already seeing the impact of changing customer expectations on the services they offer. Among our survey participants, 85 per cent believe their customers are already using FinTechs for payments, while 77 per cent believe that customers are looking to FinTechs for personal loans (globally it's only 56 per cent).

Local respondents also identified that customer preferences are making their mark on traditional financial products. Almost two-thirds (62 per cent) reported that their customers are already using FinTechs for traditional deposits/savings accounts, while 54 per cent believed customers were already using FinTechs to purchase insurance (globally it's 49 and 38 per cent respectively).

Local businesses are more sensitive to the possibility of losing customers as a result of FinTech. In fact, all of our local respondents said they are worried about increasing customer churn, compared to just 45 per cent internationally.

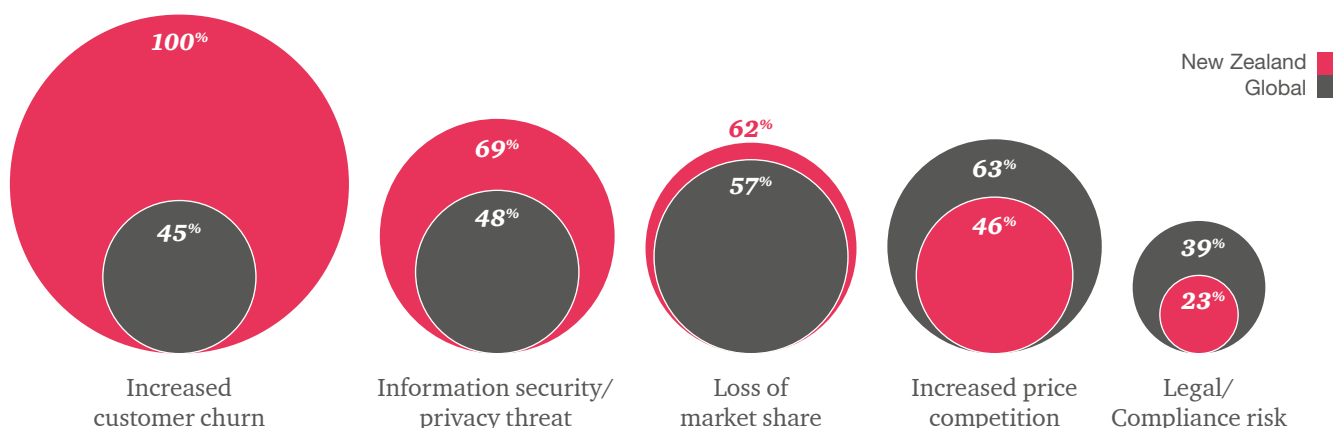
Interestingly, concern about loss of market share was much lower, and roughly in line with the percentages we recorded globally (see diagram below). It's an interesting feature of the local market that our respondents aren't worried about a shrinking market share. Instead, the real fear is that their market share becomes increasingly composed of short-term customers, requiring a greater investment in retention.

The old maxim that you're more likely to get divorced than change your bank is suddenly starting to feel less true, and it helps to explain why banks, insurers and asset and wealth management companies are investing more into their customer service and product design (see page 11).

Clearly local businesses are more sensitive to the potential loss of customers to FinTechs than their global counterparts – not surprising considering how focused our respondents were on start-ups and new competitors. However, established corporates are again running the risk of overestimating their loss of consumer influence, and underestimating their own ability to respond (or that of their competitors). Increasing customer churn will be driven as much by current incumbents as it will be by new market entrants. The companies that are successful will be the ones that can build on their existing customer relationships with a level of service that makes it easy to attract new customers and gives existing ones a reason to stay.

#### Changes on the horizon?

Q: What are the threats related to the rise of FinTech?







## Demand for digital skills

One of the stand-out findings from our 2017 CEO Survey was how important digital skills are, with a majority of NZ CEOs investing in order to achieve their growth plans. Unsurprisingly, we saw the same trend among Financial Services – 75 per cent of our respondents said they find it moderately difficult to find digital skills, while 15 per cent said it was extremely difficult.

Having access to the right skills was a huge part of the reason established Financial Services are partnering with FinTech start-ups. At the same time, though, 23 per cent of our New Zealand respondents said they find the difference in knowledge and skill sets to be a major roadblock when working with FinTechs.

A drone flying at our 2016 Platinum Series event on emerging technologies. The event explored how companies can commercialise the Essential Eight and integrate them into their products and services (see page 17).



# *Designing the next generation of Financial Services*

FinTech isn't just changing the demands customers have, it's also creating a space for established businesses to reinvent their customer-facing products and services. The benchmark for a great product experience in Financial Services has been raised, by technology companies in general that are prioritising user experience and by FinTech start-ups in particular.

We saw a pretty clear idea from established Financial Services companies on how they will respond to these changing demands from their customers. Locally, companies are placing a premium on better design of their products, rather than the speed of delivery, for example.

When we asked our local survey respondents what they thought the most important features to address were, design was the key. Almost all (95 per cent) reported that an easy-to use, intuitive product design was important, a sentiment that was shared by a majority of our global respondents. Where the findings get more interesting is in the subsequent choices. Interface and platform design, and improving product design were second and fourth priorities respectively, concerns that were far more popular here than overseas. Internationally, companies are more focused on the speed of their services, the quality of their customer care and their costs.

Driving this difference is the channels New Zealand consumers are using to interact with Financial Services. Our average respondent is engaging with 57 per cent of their client base through their website, compared to a global average of 41 per cent. Email and mobile apps were also popular (37 per cent and 35 per cent respectively), while our global respondents were more likely to rely on branches (32 per cent compared to 21 per cent locally).

Clearly, digital channels are more popular already in New Zealand, which helps to explain why product design is such a strong focus. However, the risk remains that established companies are too focused on catching up with start-ups in their product design. A FinTech start-up that is solely app-based can't provide a blue-print for redesigning the in-branch customer experience, for example.

Truly transformational product design won't just be on a single platform, it will be across all channels that a customer interacts with. Success won't come from trying to copy today's start-ups either – they're still building their channels (or deliberately avoiding those currently occupied by today's incumbents, such as branches). In many ways, established banks, insurers and asset and wealth management companies have the advantage here, but they have a long way to go if they want to reach a truly engaging, customer-centric and intuitive service offering across every channel. That's also going to take a lot more than just great product design.



## Finding room to work together

### How collaboration and partnerships are just the start of the FinTech revolution

One of the biggest changes we've seen, not just in Financial Services but across the New Zealand economy, is the increasing importance of a collaborative business approach from local companies. It's something we tracked in our CEO Survey this year, with 72 per cent of the CEOs we spoke to reporting they are looking to engage in a joint venture or strategic partnership, while 41 per cent are working with entrepreneurs and start-ups.

This trend is also playing out in Financial Services. An overwhelming majority of our respondents (85 per cent) reported they are partnering with FinTech companies, while 77 per cent are buying their services in order to improve their customer offering. Almost a quarter (23 per cent) have launched their own FinTech subsidiary, compared to just 11 per cent internationally. None of our respondents said they aren't working with FinTechs at all.

So far, the picture looks rosy, so what's holding back greater collaboration between banks and insurers, and FinTech start-ups? And could this focus on collaboration cloud the broader transformation efforts corporates have to undertake?

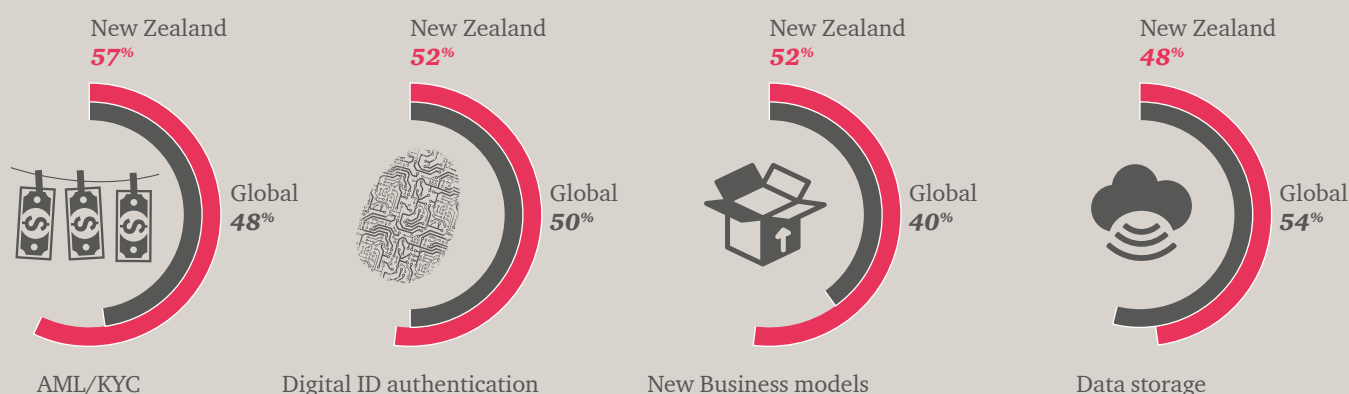
Our survey revealed that regulatory concerns are certainly pressing – both internationally and in New Zealand, 54 per cent of respondents said this is preventing them from working more closely with start-ups. However, the real difference in New Zealand isn't about regulation or technical differences, it's a difference in culture.

Differences in culture ranked as the most pressing concern in New Zealand, joint with regulation on 54 per cent. Globally, it was much lower, with only 40 per cent said it is an issue when they work with FinTechs. Divergent business models are also a major concern in New Zealand, ranking joint second with 46 per cent of respondents.

Clearly the structure of today's corporates is holding back their engagement with FinTechs, but this is far from the only reason it should be sounding alarm bells. FinTech start-ups have been designed from the ground up to be flexible, technology-driven and ultimately fit for the future. The fact that established corporates are struggling to reconcile this with their existing business model has implications far beyond their collaboration efforts.

Again, we come back to the fact that current banks, insurers and asset and wealth management companies in New Zealand are underestimating their own transformative potential – and that of their competitors. The companies that will succeed in a world of “no lines” won't just have a culture and structure that accommodates today's FinTechs. At the same time though, they won't be trying to wholesale copy the structures and culture of today's start-ups either. Instead, they'll have found the middle ground between the two, and then focused all their efforts on moving their business model and culture to that point.

Q: In which areas do you see regulatory barriers to innovation in FinTech?



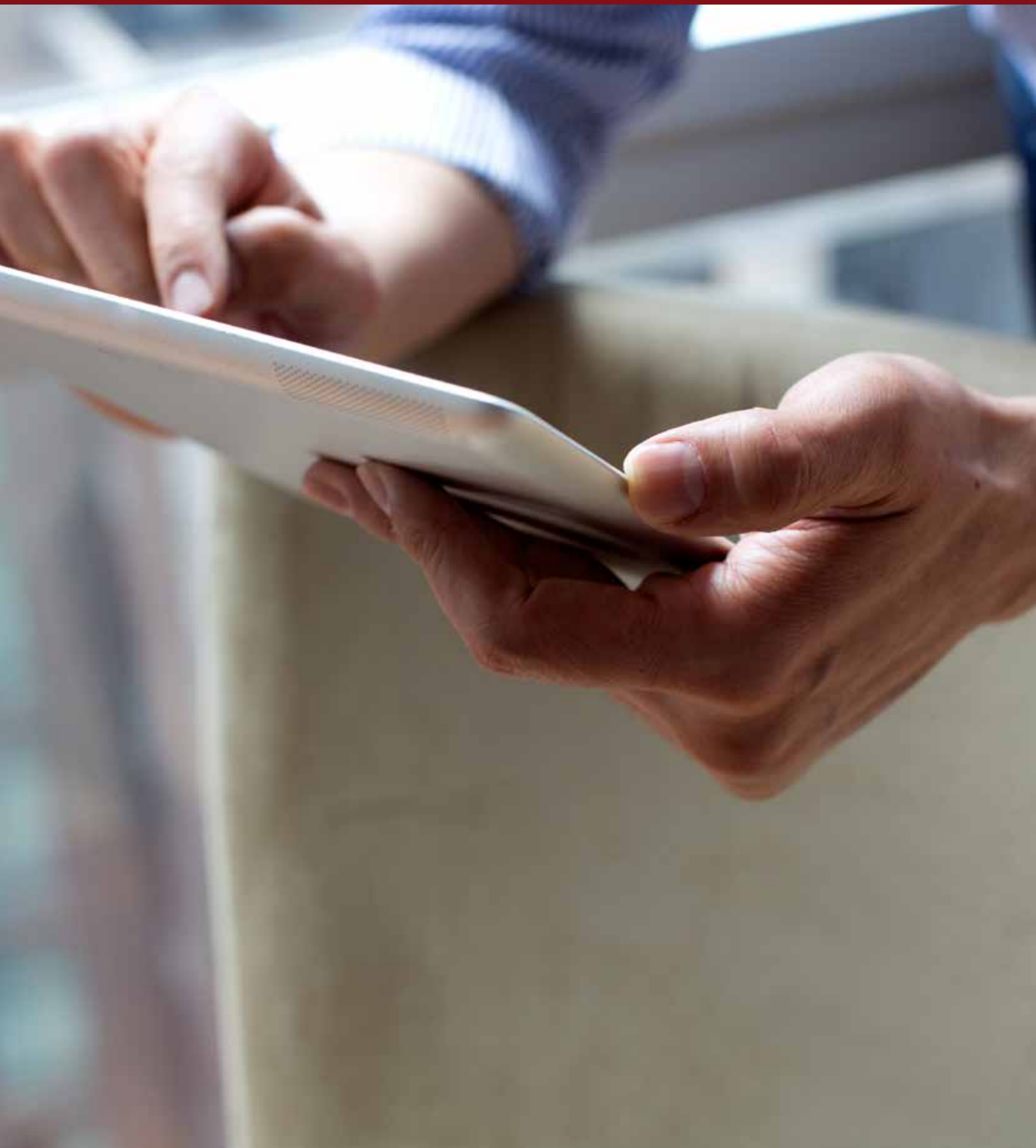
## What are the regulatory barriers to innovation?

In New Zealand, our respondents are worried about how anti-money laundering (AML) and know your customer (KYC) processes will be regulated. Interestingly, the leading concern globally is around data storage, privacy and protection, issues that collectively ranked fourth locally.

**85%**

*of New Zealand respondents are  
already partnering with FinTechs*







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## ***Expanding banking: how FinTech is creating new opportunities for underserved customers***

As well as our broader Financial Services findings, our 2017 FinTech survey also contained a number of key findings specifically for the banking sector.

Looking to the next five years, we asked our banking respondents what they see as the most important FinTech trends they face. The most pressing here was the changes in customer preferences that the sector is seeing, with 62 per cent stating that increasing customer empowerment and control over their finances will be very important through to 2022.

In equal-second place on 54 per cent was the emergence of new services that meet the needs of unserved – or underserved – banking customers. This is especially relevant for the local banking market, where we have already seen a high level of market penetration for banking services. In an already mature market, carving out new customer segments using technology will be incredibly lucrative for those companies that can do this well. Interestingly, the other area that is equally important for our banking respondents was operational: 54 per cent said it would be very important to integrate digital solutions into their operations.

Unsurprisingly, these two areas of customer and operations are also going to see the greatest investment from banks. Over three-quarters of our respondents (77 per cent) reported they are very likely to devote resources towards customer empowerment in the next five years. Likewise, 69 per cent are investing in digitising their back-office operations.

For banks, FinTech isn't just a chance to build stronger, deeper relationships with clients, it's a chance to build a broader client base, offering new products as part of a broader ecosystem of Financial Services that form a consistent customer experience. There are certainly lessons here that banks can learn from FinTech start-ups, but offering a range of traditional and new products to a broad consumer base can only come from an established bank – for now.

## Putting the Tech in FinTech

### The innovations driving change in Financial Services

So we've established how technological change in Financial Services will come from all sides, not just from start-ups but from today's established banks, insurers and asset and wealth management companies as well. The question remains, though: which technologies are corporates going to be using as they drive towards this hybrid Financial Services model?

As we discussed on page 11, local companies are seeing the majority of their client interactions through their website, with email and mobile applications rounding out the top three. In-person interactions through a branch were much lower.

At first glance, it would be easy to say that New Zealand customers are taking a digital-first approach compared to their global colleagues, but there's considerable variation among local companies in the technologies they are investing in.

Mobile apps ranked third for current client interactions, and is the platform that will see the greatest investment over the coming years. Almost all (86 per cent) of our survey participants reported they will see growth in mobile apps over the next five years, compared to 81 per cent for website and 71 per cent for social media. Only 5 per cent are expecting growth from branches, compared to 12 per cent internationally. Unsurprisingly, mobile also ranked as the second-most important technology for companies to invest in, trailing only data analytics.

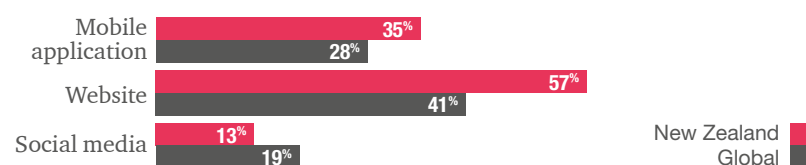
Given the importance of data, it's no surprise that leveraging data and analytics was the key opportunity that the rise in FinTechs have seen, rivalled only by the ability to differentiate their services (see page 6). The increasing role of technology among customer interactions means companies have access to more data than ever. The challenge for incumbents is to turn this into a foundation of information that actually informs decision-making.

While FinTech has driven the importance of data and analytics, it isn't necessarily FinTech start-ups that are offering the best models for using it. Current FinTechs may be winning customers and building services that incorporate data analytics, but they will be working with far fewer data collection points than an established institution.

The challenge for today's FinTech start-up will be to scale their existing processes to handle more data from an increasing number of customer channels. Today's incumbents instead have to start from a position where they are already incredibly data-rich. They therefore have to scale their data analytics out across the business, rather than scale up like a maturing start-up will.

#### Customer interactions go digital

Q: What percentage of your clients do you interact with through the following channels?



#### Mobile leads for future growth

Q: Which channels do you expect the largest growth in usage over the next 5 years?





## The Essential Eight and FinTech

For many of our FinTech respondents, the tools they are investing in aren't new. Social media, mobile apps and their websites are now well-established tools that customers are comfortable with and well-versed in.

Emerging technology, like the Essential Eight we identified in our *2016 Tech Breakthroughs Megatrend report*, are now making their mark. You can read more about our in-depth findings for just one of those technologies – Blockchain – on the next page.

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Those eight technologies are:



*Artificial Intelligence*



*Blockchain*



*Augmented Reality*



*Virtual Reality*



*Drones*



*Robots*



*3D Printing*



*The Internet of Things*

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These eight will transform every sector, especially Financial Services. Autonomous vehicles, for example, sit between robotics and the Internet of Things, and will have huge implications for the insurance sector. Likewise, artificial intelligence is completely reshaping the way banks engage with customers, through the use of chatbots, for example. It's these eight that will underpin the next generation of FinTech products, and today's incumbents have to be getting comfortable with them now, if they want to harness their potential tomorrow.

## Who's top of the Blockchain?

### Digital identity management the focus for blockchain in New Zealand

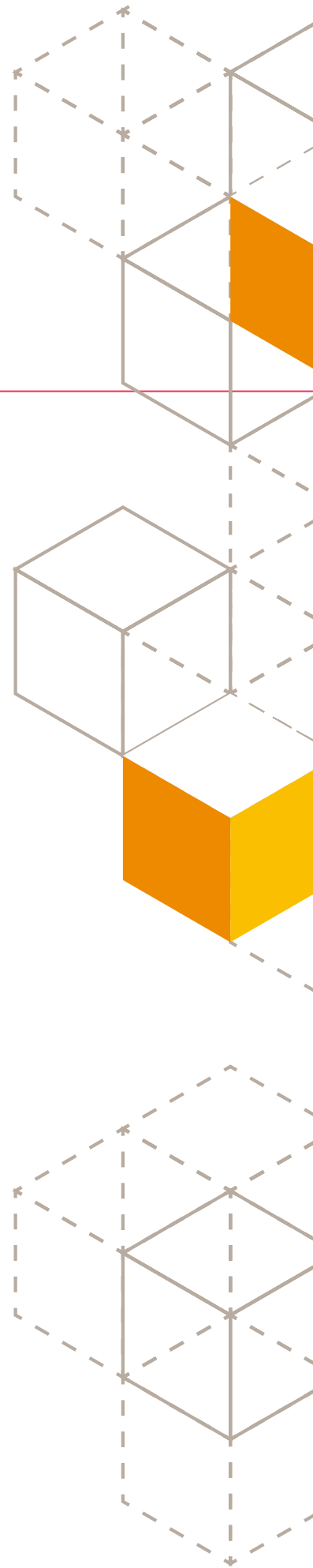
Blockchain is coming in to its own here in New Zealand. Last year, the Blockchain Association New Zealand opened its doors and the technology has been an increasingly important part of the FinTech revolution. As one of the Essential Eight emerging technologies, we're expecting Blockchain to significantly change the way we think about Financial Services.

Despite this, Blockchain adoption locally is lagging behind our overseas counterparts, many of which have adopted regulatory and policy changes to encourage the deployment Blockchain technology. Just last year Australia's Commonwealth Bank and Wells Fargo in the USA conducted the world's first open account transaction using Blockchain technology.<sup>1</sup> Facilitating this growth overseas has been the rise of "regulatory sandboxes" in countries like the UK<sup>2</sup> and Singapore<sup>3</sup> that streamline the licencing and compliance requirements for FinTechs.

So how will Blockchain shape the New Zealand market? Our survey participants actually pointed to one area where there is the greatest potential for this technology: digital and identity management. This, along with payment infrastructure, were the two most common business use cases we saw (65 per cent each), compared to 55 and 46 per cent among our global survey pool.

Interestingly, there were also a number of areas where Blockchain isn't picked to have as great an impact. Trade finance and regulatory compliance were two areas where our respondents were less likely to identify a business use case for Blockchain technologies.

1. For more on the Commonwealth Bank experiment, you can see the full announcement here: <https://www.commbank.com.au/guidance/newsroom/CBA-Wells-Fargo-blockchain-experiment-201610.html>  
2. See: <https://www.fca.org.uk/firms/fintech-and-innovative-businesses> for more on the UK's regulatory sandbox model.  
3. See: <http://www.mas.gov.sg/~media/Smart%20Financial%20Centre/Sandbox/FinTech%20Regulatory%20Sandbox%20Guidelines.pdf> for more on the Singapore government's FinTech regulatory sandbox guidelines.







## *Insurers join the Blockchain party*

While Blockchain is making its mark across Financial Services, there are some areas that are more at risk than others. In the insurance sector, for example, companies are looking to apply Blockchain technologies to improve internal processes and the quality of data the company has.

When we asked insurers where they saw Blockchain having the greatest impact, the leading response was in advanced information security. The ability to predict, detect and analyse fraud is a key concern, one that all of our insurance respondents said would be affecting their organisation over the next five years. Insurers are responding as well: 72 per cent said they would likely be devoting resources to this in the next five years.

On the other side of the ledger, many of our insurance respondents are looking to invest in Blockchain technology for attestation, audit, record keeping and data integrity. In fact, 57 per cent of our respondents think they will likely be investing in this technology over the next five years.

The growing awareness and interest in these applications of Blockchain technology point to the broader uses of the technology beyond early examples like cryptocurrencies. For insurers, many of the most valuable applications of Blockchain technology will be in back-end systems that allow for greater transparency and information security compared to current centralised systems.

Blockchain is also just one part of the broader InsurTech revolution. Whereas other sectors are seeing the rise of FinTechs as a challenge to their customer-facing interactions, for insurers the real change will be to their internal processes. This new generation of tools that can model data and quantify risk in new ways will have massive implications for the insurance sector. Regardless of the role Blockchain plays in this change, there's no doubt that this new generation of InsurTech services will make a huge difference to the way incumbent insurers operate.





## What's next?

### Creating a two-speed innovation strategy for the FinTech revolution.

For today's corporates, FinTech start-ups aren't just nibbling away at their margins, they're uncovering completely new markets, pockets of underserved customers and new products and services. Today, they might only be targeting a small niche – for example the wealth management FinTech offering AI-powered investment advice to those who don't have the assets for a traditional financial advisor. But it's only a matter of time before that start-up matures and has the scope to offer one-on-one human advice as an add-on to their AI offering.

Clearly today's corporates have to look beyond simply partnering with FinTechs if they are going to navigate the next five years of change within the sector. Striking that balance requires thinking deeply about the new opportunities that FinTechs are unlocking, but also working on their own internal innovation capabilities.

This two-speed innovation strategy brings together the best of both worlds – the existing expertise of today's corporates with the innovation, creativity and digitally enabled business models of today's start-ups. It's a blueprint for that transition to a hybrid Financial Services firm, that can move and change like a start-up, but that has the breadth of services that are currently held by Financial Services institutions.

#### A two-speed FinTech innovation strategy

##### **Internal capabilities:**

- Build a culture that is both compatible with start-ups but that also fosters innovation internally.
- Focus on the skills in your organisation, especially digital, creativity and innovation. Don't just rely on FinTechs for these skills.
- Build internal awareness and capability around emerging technologies and incorporate this into the broader FinTech strategy.

##### **Partnering with FinTech start-ups:**

- Focus on partnering with FinTechs that can create a point of difference in the marketplace.
- Beyond developing new products and services, use FinTech partnerships as a chance to learn and inform your own internal innovation strategy.
- Recognise the strengths that FinTechs can bring in areas like product design and data and analytics and apply these lessons across all customer touch points.

*Today's Financial Services incumbents can't underestimate the scope of this transformation. The FinTech revolution won't happen overnight, but it will happen – and companies of every size across Financial Services have to be ready for it.*

## Contacts

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The 2017 Global FinTech survey was based on the responses of 1,308 participants, principally chief executive officers (CEOs), directors/department heads, heads of IT/digital/technology, and other top management involved in strategy and innovation from 71 countries and across six regions.

Of that global survey pool we had 22 New Zealand respondents, split across banks, insurers, asset and wealth managers and FinTech start-ups.

