

## **Commentary: Digital Banking in Asia**

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### **The Big Picture**

In the latest McKinsey report: "Retail Banking in Asia – Actionable Insights for New Opportunities"<sup>1</sup>, it estimated that Asia will reach over US\$ 900B in retail banking by the end of the decade with an average 14% growth per year from 2010. The report also projected that the region will be the second largest wealth management footprint globally after the US and with even more personal financial assets residing in Asian compared to Europe by 2015.

While investment analysts and investors continued to be optimistic on the growth of Asia over the longer term, the Asian Development Bank's latest Pacific Economic Monitor<sup>2</sup> has trimmed the 2013 economic growth forecast for the Pacific region to 5% down from 5.2%. Meanwhile, the Jun 2013 Asia Pacific Economic Outlook<sup>3</sup> by Deloitte University Press reported that China, the main growth engine in Asia is expected to grow at an even lower average 7.0% per year for the remainder of the decade. This is in contrast to the 7.5% growth projected for this year which is down from 7.8% in 2012.

Indonesia, the world's largest exporter of palm oil and thermal coal, among other items is another emerging Asian country that has shown promising economic growth over the past few years. This week, the World Bank has cut its forecast for the country to 5.9% compared to an earlier forecast of 6.2%. Against these recent developments, banks such as DBS Bank continued to pursue presence in Indonesia for greater penetration into its domestic banking sectors; particularly in the retail banking and financial services for small and medium enterprises.

### **Digital Banking in Asia**

Although the McKinsey's report covers 8 topics ranging from innovation, branch obsolescence, customer-centricity and more to private banking markets in Asia; this commentary is focused on digital banking in Asia given the exponential growth in internet in Asian countries over the last decade. According to Mediabuzz<sup>4</sup>, there are over 1 billion online users (46% of the world's total) across Asia Pacific with more than half (513 million) in China. In addition, 623 million people access the web via their mobile phones.

These projections point towards positive catalysts for digital banking in Asia: firstly, the high level of internet penetration complemented by web access via the mobile phone will drive more online purchases and ecommerce which eventually will require payment related services. Secondly, market research firm, eMarketer<sup>5</sup> released a report late last month claiming that Business-to-Consumer (B2C) ecommerce will grow by 17% globally in 2013 with the Asia-Pacific region not only driving ecommerce growth but is expected to outpace the rest of the world with 23% growth over last year. As Asian internet users become more familiar with online purchases for goods and merchandise, the existing barriers on procuring financial services online are expected to be less inhibitive.

McKinsey's report mentioned that customer expectation in Asian and Western markets are converging on many important points and one visible observation was the technology-savvy and self-directed customers are the earliest adopters. While this observation is still valid from a macro perspective, further examination going by the experience of one of the largest Asian banks, DBS Bank<sup>6</sup> revealed that the

younger and tech savvy customers are no longer the main users of the Internet banking service as senior citizens (age 55 years and above) and the High Networth (HNW) customers are increasing using the bank's internet banking launched since late 1997.

### **Late Comers are not (always) Losers**

Moreover, given the different economic conditions, progress made in infrastructure developments and political situation, Asian countries are at different phases of banking developments. Hence, the population being offered or taking up banking services are in varied stages and readiness. For instance, while branch and ATM penetrations are high in countries such as Japan, Hong Kong, South Korea, Singapore; the lack of telecommunication infrastructures have resulted in scarce bank branches and remote ATMs in outskirt cities in countries such as Indonesia, India, Pakistan and Sri Lanka.

Although some of these countries lacked in landline infrastructure, they have leap-frogged in wireless communication development compared to their developed counterparts in Asia. As a result, mobile phones have flourished in countries from Vietnam to remote villages in India with short-messaging system (SMS) being a common infrastructure used for payments and basic banking transfer services. Although critics of SMS banking have often highlighted the unsecured SMS infrastructure and the technology used, many major banks in India that offered various forms of SMS banking to complement their lack of customer touch-points due to the geographical spread and infrastructure constraints have adopted various types of compensating controls such as pre-registrations, limit the amount of financial transactions and alert notifications. Banks in India that have successfully implemented SMS banking include Union Bank of India, ICICI Bank, HDFC Bank, Axis Bank.

While Near-Field Communication (NFC) has often been touted as the emerging technology that will revolutionised mobile payment and make payment using the mobile device more convenient and secured, this author had in Feb 2009<sup>7</sup> written that simple but well established technology such as the SMS could still be leveraged upon for specific needs. Web 2.0 and its suite of web technologies will be very useful to build Bank 2.0 and beyond but each bank would need to review its customer base, assess their needs and readiness for embracing new technologies. Many banks are fully aware that replacing savings passbook with statement and e-statement accounts often take more than 1 decade as technology was never the inhibitor in the first place.

There is another reason why incumbents are always not so ready to adopt newer technology – migration from existing legacy systems. When a major ATM vendor was releasing its newer generation of ATMs back in 2005-2006 that are equipped with higher resolution touch screen, programmable codes amongst other features; many banks in Singapore were unable to migrate to these new machines quickly because they have an existing network of older machines and operation platform that must be phased out over a period of time due to financial and other considerations. In contrast, some banks in Vietnam were able to leap-frog and ordered this newer generation of ATMs because they don't have an existing baggage to worry about. However, integrating these machines into their Retail Banking blueprint, operating and maintaining them become key challenges for these new comers – this is another story outside the scope of the current discussion.

### **Shaping the Governance Framework**

The chapter on "Digital Banking in Asia" in the McKinsey report noted that banks in Asia should be mindful of attackers from start-ups like Square to longtime giants Google and PayPal that have encroached on traditional banking territory, especially

using digital payment as the main point of entry. This is a definitely one key consideration that Asian banks must always be watching out for which is further amplified by the lack of more established regulatory framework in emerging markets to govern the interactions between the various participants: banks, network providers, equipment manufacturers, merchants and payment service providers.

In a Working Group Report released by the Bank for International Settlement: "Innovations in Retail Payments" last year<sup>8</sup>, it highlighted that central banks will face numerous challenges in striking a balance between imposing regulations and encouraging innovations in retail payments. Some of the key challenges include understanding risks and other implications brought about by newer payment technologies, the need to promote inter-operability and inter-connectivity with other systems, co-operation with other central authorities, impact on central bank's other operations and most importantly how cash will be affected as more services become digital.

For digital banking to take off in Asia, retail banks with regional footprint would do well by participating early and contributing in national bodies or working committees that have been given mandate to consult the industry and shape the outcome of how digital banking should operate and the types of governance structures that are to be put in place.

There is an old Oklahoma saying that sums up the need to influence policy development very well: "If you are not at the table; you are on the menu." Any retail bank would know that regulations of any sort would create business opportunities for some while inhibiting growth of others. To remain competitive, retail banks should constantly monitor developments of both banks and non-banks and participate actively in the regulation consultation processes.

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## Notes:

<sup>1</sup> McKinsey & Company: "Retail Banking in Asia – Actionable Insights for New Opportunities":

[http://www.mckinsey.com/insights/financial\\_services/navigating\\_the\\_new\\_era\\_of\\_asian\\_retail\\_banking](http://www.mckinsey.com/insights/financial_services/navigating_the_new_era_of_asian_retail_banking)

<sup>2</sup> Asian Development Bank: Pacific Economic Monitor at: <http://www.adb.org/news/adb-trims-pacific-2013-economic-outlook-risks-growth-emerge>

<sup>3</sup> Deloitte University Press: Asia Pacific Economic Outlook Jun 2013:

[http://www.deloitte.com/assets/Dcom-](http://www.deloitte.com/assets/Dcom-Indonesia/Local%20Assets/Documents/APAC%20Economic%20Outlook%202013/APAC_June13.pdf)

[Indonesia/Local%20Assets/Documents/APAC%20Economic%20Outlook%202013/APAC\\_June13.pdf](http://www.deloitte.com/assets/Dcom-Indonesia/Local%20Assets/Documents/APAC%20Economic%20Outlook%202013/APAC_June13.pdf)

<sup>4</sup> Mediabuzz: Digital Marketing Trends 2013: [http://www.mediabuzz.com.sg/asian-emarketing/Digital-](http://www.mediabuzz.com.sg/asian-emarketing/Digital-Mktg-Treads-2013/1817-adma-digital-marketing-yearbook-2012-in-retrospect)

[Mktg-Treads-2013/1817-adma-digital-marketing-yearbook-2012-in-retrospect](http://www.mediabuzz.com.sg/asian-emarketing/Digital-Mktg-Treads-2013/1817-adma-digital-marketing-yearbook-2012-in-retrospect)

<sup>5</sup> eMarketer on eCommerce: [http://thediplomat.com/tech-biz/2013/06/29/b2c-ecommerce-could-top-1-2-](http://thediplomat.com/tech-biz/2013/06/29/b2c-ecommerce-could-top-1-2-trillion-driven-by-asia-pacific-growth/)

[trillion-driven-by-asia-pacific-growth/](http://thediplomat.com/tech-biz/2013/06/29/b2c-ecommerce-could-top-1-2-trillion-driven-by-asia-pacific-growth/)

<sup>6</sup> Sherman Tan, Innovar Pte Ltd: Branchless Banking, May 2013:

[http://www.innovar.com.sg/more.htm#Branchless\\_Banking](http://www.innovar.com.sg/more.htm#Branchless_Banking)

<sup>7</sup> Sherman Tan, Innovar Pte Ltd: Will NFC revives Mobile Payment, Feb 2009:

[http://www.innovar.com.sg/Archives/Will%20NFC%20revives%20mobile%20payment\\_27Feb09.pdf](http://www.innovar.com.sg/Archives/Will%20NFC%20revives%20mobile%20payment_27Feb09.pdf)

<sup>8</sup> Bank for International Settlement: "Innovations in Retail Payments":

<http://www.bis.org/publ/cpss102.htm>

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