

IRISH 2021 OUTLOOK FOR

BANKING & CAPITAL MARKETS

- PRESSING THE RESET BUTTON -



SEAN SMITH
PARTNER, BANKING LEADER
Deloitte Ireland

If we wind the clocks back to the beginning of 2020, many banks would have identified pandemic risk on their risk register, but few would have rated its likelihood high on that list. So when COVID-19 struck Europe during the first quarter of last year it meant that banks not only had to navigate a novel and extremely challenging situation, they also had to reassess their business model and the threats to that business. Possibly shaped by their experiences in the financial crisis of 2008, we saw many Irish banks take a cautious and prudent approach whereas we saw many EU banks continue to invest and drive strategic change, particularly where this would give an advantage in the post-pandemic world.

With digital penetration significantly increasing, more banks are looking at digital in a holistic way to serve their customers – giving the customer the experience they want rather than the process that works best for the bank.

In some ways, COVID-19 has accelerated trends that had been happening in banking anyway. All banks have struggled with profitability during a sustained period of low interest rates. The arrival of new types of competitors also predates the pandemic. But seen from another perspective, the sudden and drastic changes wrought by the crisis are a useful moment for banks to take stock, and even hit the reset button and embark on a different path. Below, we outline some of the key considerations for banks over the coming year.

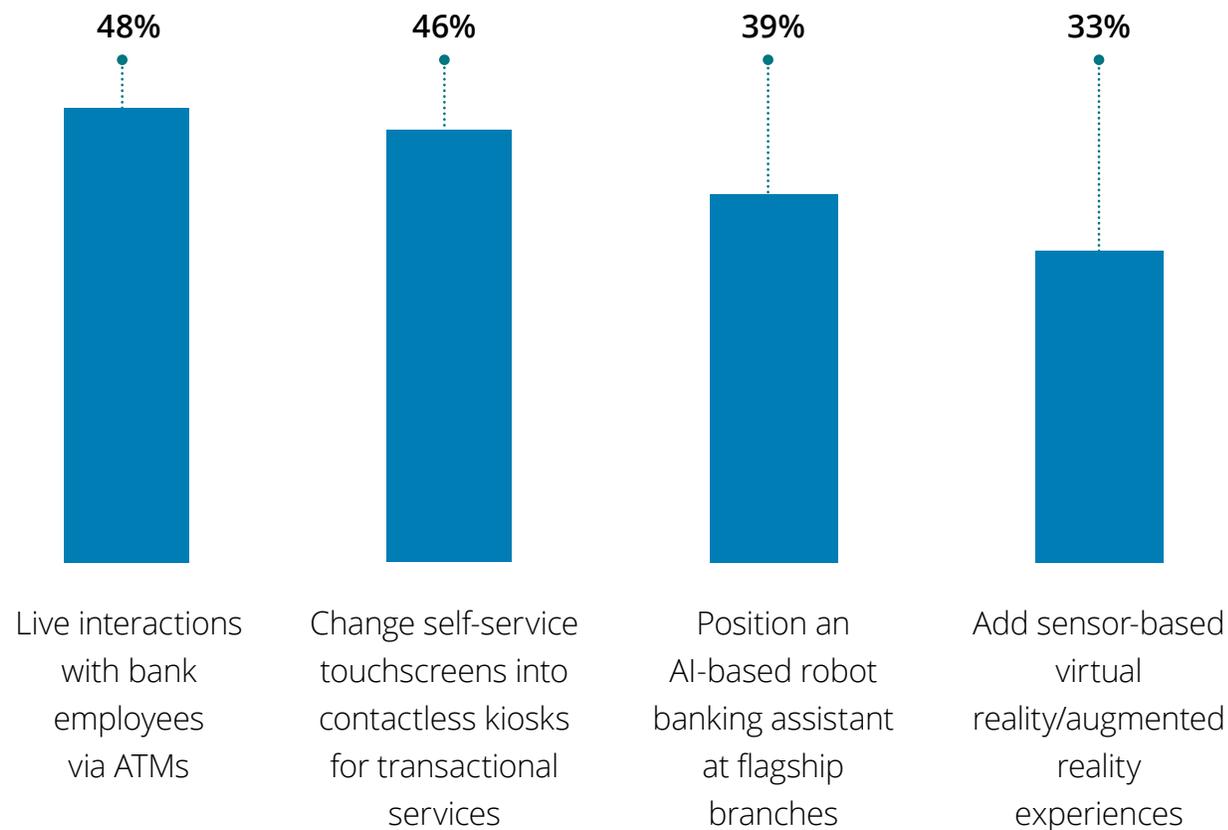
Digital embrace continues at pace

In the past, many banks struggled to achieve widespread penetration of digital channels among their customer base, partly because different segments of society were reluctant to use them. COVID-19 changed all that, because restrictions on movement during lockdowns effectively forced people to go online. The firms that had invested more in digital were able to manage this process more efficiently and were successful in the early days of lockdown.

With digital penetration significantly increasing, more banks are looking at digital in a holistic way to serve their customers – giving the customer the experience they want rather than the process that works best for the bank. Although there will always be a portion of the customer base that want to visit banks in person, I expect to see more of them being repurposed to digital hubs and a lot more customers doing most of their banking online. Hyper-personalisation will be key as will be the technology that can identify suitable and appropriate products for customers and treating vulnerable customers appropriately. As the Deloitte Global Outlook Survey has shown, some banks are considering a number of digital capabilities for their branches over the coming year.

Figure 1. Some banks will add more digital capabilities to branches over the next year.

Digital changes being considered



Cost efficiency

In an environment where extremely low interest rates challenge profitability, banks must turn to what they can control: cost. This doesn't mean cutting all cost but rather developing a clearer understanding of the bank's return on spend across the business vertically and horizontally. Investment will be crucial for banks to adapt to the coming challenges, further driving the imperative to cut unprofitable businesses, products or processes to allow for future growth. Efficiencies of scale need to be considered also and we expect some significant M&A activity and asset sales/acquisitions over the coming year.

Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Figure 2. How COVID-19 has affected megatrends globally



Digitisation

Social distancing has already driven further **adoption of contactless technologies and digital experiences.**



Virtualisation of the workforce

Many **organisations have already adjusted to working remotely**; COVID-19 has led to **increased adoption of flexible workplace models.**



Focus on safety and surveillance

More **consumers will likely expect safety and precautionary measures from both brands and governments.**



Corporate responsibility

Taking steps to do the right thing in the COVID-19 context is becoming **table stakes for consumers.** The larger **purpose of banks is changing.**



Emergence of pop-up ecosystems

Value chain disruption will likely result in **more creative partnerships**, innovation, and agility.



Focus on cost reduction

Structural cost reduction could be a critical priority to ensure business continuity based on cash, profits, and revenues.



The sharing economy

Rising health and hygiene concerns and increased virtual work may **reduce demand for shared services.**



Urbanisation

While urbanisation has been growing steadily, **social distancing and rising fears of contagion may reduce the likelihood of people living and working in major cities.**



Global movement of people and goods

Based on likely government restrictions, the **movement of people and goods across national borders could decrease.**

■ Accelerated ■ Decelerated

A greater focus on fee-based products and alternative business models

After the financial crisis, banks had to divest sides of the business that derived fee-based income. Now, some banks will need to diversify their products – for example, bringing pension products to the fore – in order to stay competitive and to offer the end-to-end product set that customers now expect. This mirrors what is happening with fintech startups that are combining traditional banking services with cryptocurrency investment, for example. Other business models such as banking as a service, payments and bancassurance have also come on the agenda for banks looking to grow their offering.

All eyes on customer experience

Another aspect of embracing a digital strategy is how it meets the need to enhance their customer experience in a way that makes it easy and seamless for clients to interact. This is a kind of virtuous circle: the easier it is to do business with a bank via digital channels, the more customers will want to use those channels.

The agility agenda

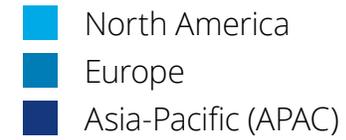
Ultimately, the bigger question for banks' digital strategies is whether to approach it as a layer on top of their existing platforms or carry out a deeper upgrade of their core systems. Banks that approach this question as simply a matter of adding a slick 'front end' are likely to reach a point in the process where their lack of agility could create issues, slowing down their ability to provide new services or manage their costs.

Some clients have chosen to tackle this by effectively building a separate 'digital' bank, running on different infrastructure. This has several advantages: newer technology is better able to meet the goals of resilience and agility, while there are many cost and speed benefits of setting up a greenfield operation.

COVID-19 may also lead to quicker adoption of cloud technology. In our experience, this is usually more successful in delivering agility than achieving cost savings. Financial regulators have historically looked at the cloud with some unease, but the drastic and sudden changes triggered by the COVID-19 crisis has encouraged them to engage more on this issue. We can expect to see a softening of their stance over time as banks demonstrate the reliability and security of cloud and regulators become more comfortable (possibly even regulating the cloud providers). This is likely to be a positive development for banks' digital strategies.

Figure 3. Banks plan to take a variety of actions to support financial and operational stability

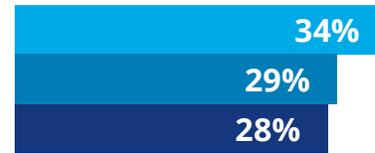
Actions planned over the next 6–12 months



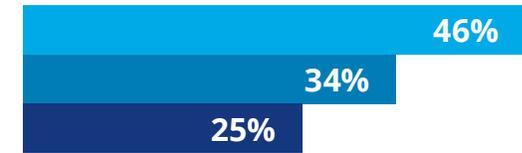
Implement technology to enhance efficiency



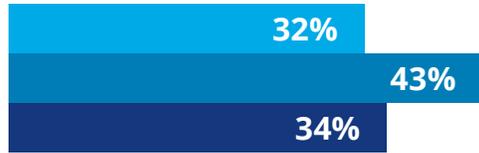
Divest nonperforming or noncore operations



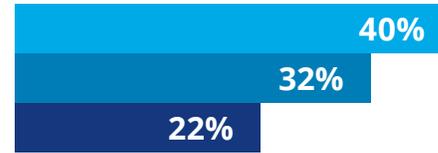
Rationalise compensation and headcount



Rationalise assets



Trim discretionary spending



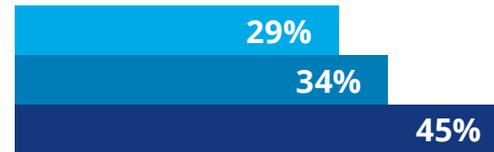
Suspend new expenditures and investments



Pursue mergers or acquisitions



Accelerate innovation initiatives



Rationalise real estate footprint

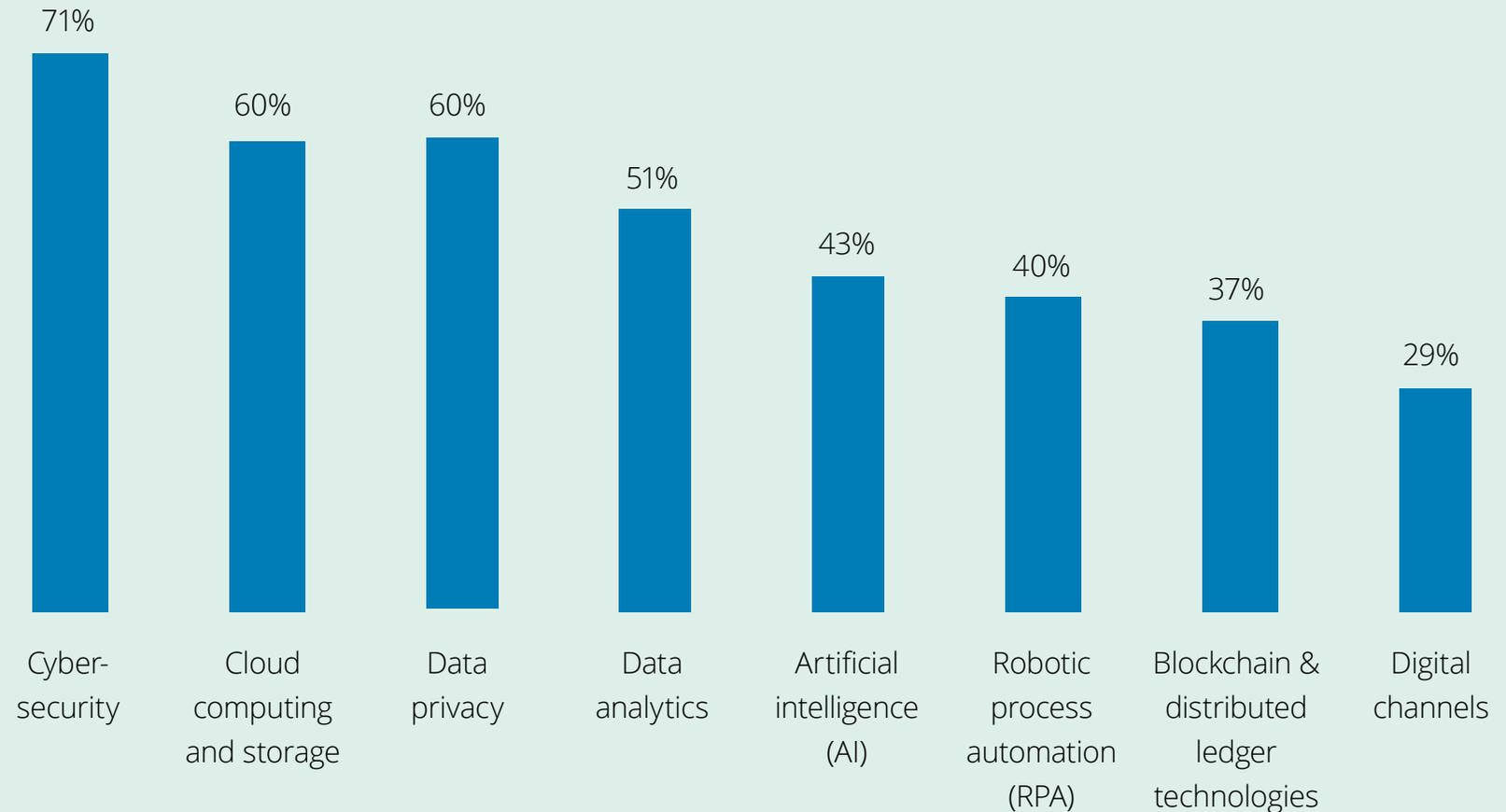


Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

The sudden and drastic changes wrought by the crisis are a useful moment for banks to take stock, and even hit the reset button and embark on a different path.

Figure 4. Banks plan to increase spending on various technologies over the next year

Finance respondents whose organisations plan to increase spending



Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.



Operational resilience

COVID-19 has focused minds on business continuity and the need for greater operational resilience. If a pandemic can happen, then it's not outside the realms of possibility that a system crash, cyber-attack or other event could bring business to a standstill – permanently. Operational resilience focuses not only on your ability to respond to such catastrophic events; it also puts a premium on prevention over cure. For these reasons, it is not surprising that cybersecurity (71%) and cloud (60%) scored highest in Deloitte's global survey of financial firms' planned spending. Both areas directly address the resilience agenda.

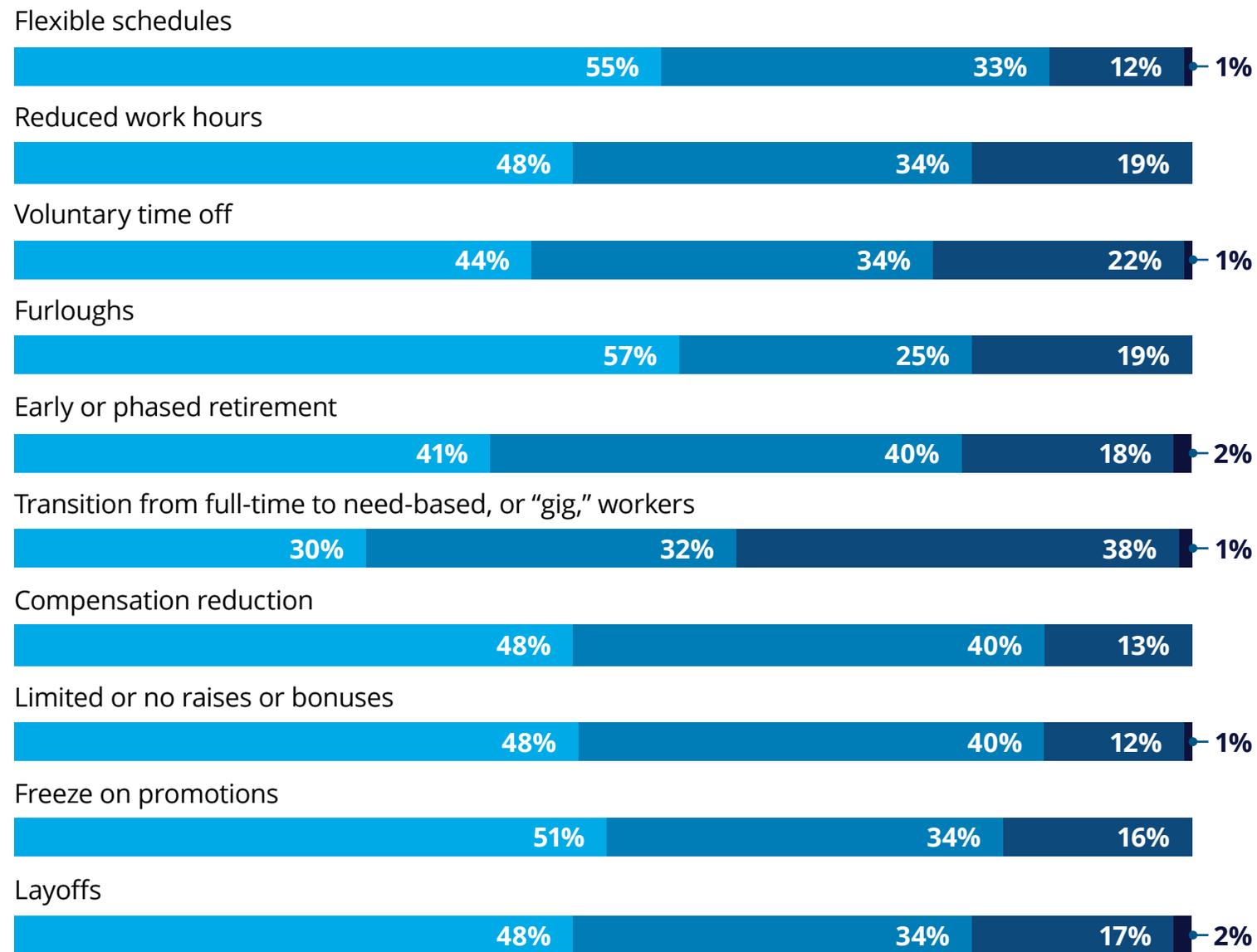
The talent question

There have been job losses as banks adapt and try to right size for the new environment, but the deep nature of the move to digital, and the restructuring it requires, will force banks to re-evaluate their talent strategy. In the digital world, the formula for competing with new fintech players and payment providers is likely to involve fewer people and more technology. The roles themselves will change, with banks increasingly needing more software engineers than bank tellers. While many banks are already facing this challenge, we feel it will become more pronounced over the coming years. This means that banks will be competing more regularly for talent with technology companies and social media giants. Are banks an attractive recruitment proposition by comparison? Or can they identify suitable candidates for reskilling for this new world from within their existing teams? Deloitte's Global Outlook survey sheds light on actions that banks have taken to date in adjusting their employment plans.

Figure 5. Banks continue to make talent changes in response to COVID-19

Employment actions taken to date

- Have already implemented
- Planning to implement
- Have not implemented and not planning to
- Don't know



Source: The Deloitte Center for Financial Services Global Outlook Survey 2020.

Conclusion

For the past number of years, banks have been somewhat caught in the middle between low interest rates and limited ability to launch new products that will make a difference to their profitability.

In a way, for all the many challenges brought about by the COVID-19 crisis, it has also created a series of new directions the banks can start to follow. It has allowed digital to make long overdue progress. The enforced moves to remote working have opened up questions about the need for large, centralised offices or extensive branch networks. Questions that were never on the table before are suddenly up for discussion.

From a strategic standpoint, banks can see 2020 as a reset button. It has given them permission to examine some things they couldn't look at before. As we look ahead to 2021 and beyond, the change is not over; it is just beginning. At the time of writing, we are still dealing with a heavy

surge of COVID-19, while the ink is still drying on the eleventh-hour Brexit agreement. Now banks must focus on how to navigate the current uncertainty and emerge from it in the hope of remaining attractive to analysts and investors while supporting their customers and meeting regulatory expectations.



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**2021 Banking and
Capital Markets Outlook**

