RETAIL BANKING
TOP TRENDS 2024

CONTENTS

FOREWORD

As we enter 2024, the global economy remains sluggish. While record interest rate hikes punctuated the last 12 months, increasing the cost of money, inflation continues above target levels, increasing the cost of living. While overall the banking industry did well in 2023, the retail banking sector took a hit in deposits.

Retail banks are prioritizing efficiency and cost management as a hedge against macroeconomic and geopolitical uncertainty. With several banks failing in 2023, customer trust is challenged, triggering a mass outflow of deposits and a general test of deposit stickiness.

To attract customers and remain resilient, retail banks are offering aggressive deposit rates. Thanks to lower overhead and with a focus on increasing market share, new-age e-banks are particularly generous with high savings rates. While higher deposit rates are likely to continue, a significant move to time deposits is underway which makes it even more critical for banks to manage operational costs innovatively.

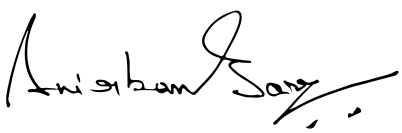
Banking sector technology continued rapid development throughout 2023, with much buzz around generative artificial intelligence (AI). Having become a priority for executives almost overnight, generative AI holds promise to reimagine numerous banking functions.

Initially spearheaded in Europe, open banking is gathering global steam as customers embrace the convenience, retail-like shopping experiences, and control over personal data it enables. While banks continue to migrate to cloud-powered platforms, we believe edge servers will reduce latency and bandwidth consumption while allowing data sovereignty in accordance with the laws of the jurisdictions where data is generated or collected. On the sustainability front in 2024, we expect more banks to leverage environmental, social, and governance (ESG) data beyond regulatory reporting to inform strategic decision-making and unlock business value.

Regulators continue tightening compliance mandates, forcing banks to defend against financial fraud more effectively and to shore up digital operational resilience. And emerging regulations around decentralized finance may help build the trust necessary to reignite sector development.

While the storm is not over, banks have become savvy navigators of turbulent macroeconomic seas. They must continue to remain agile, resilient, and innovative to weather the storm and usher in the next phase of growth.

I hope you find our Retail Banking Top Trends 2024 to be insightful as you launch initiatives in the new year.



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INTRODUCTION

MARKET DYNAMICS

As we begin 2024, banking industry challenges persist, including the impact of a sluggish global economy, intense competition for customer deposits, and the necessity for cost management and containment. Turbulence drivers include high interest rates, reduced money supply, stringent regulations, and geopolitical tensions.

- The International Monetary Fund suggested in Q4 2023 that policy tightening measures are beginning to yield results and moderate economic fluctuation, although core inflation remains persistent. The report forecasts a decline in global inflation from 2022's 8.7% to 6.8% in 2023 and 5.2% in 2024.[1]
- Over the past two years, central banks worldwide have unleashed a series of steep interest rate hikes to control inflation. In advanced economies since 2021, interest rates have risen approximately 400 basis points, with emerging market economies up around 650 basis points.[2]
- In the United States in 2023, First Republic Bank, Silicon Valley Bank, Signature Bank, Heartland Tri-State Bank, and Citizens Bank underwent debilitating financial failure as European banking giant Credit Suisse collapsed and was absorbed by UBS. These bank collapses triggered a substantial withdrawal of deposits: according to US Federal Reserve data, Americans withdrew USD 98.4 billion from their bank accounts on a seasonally adjusted basis.[3]
- The 2023 triple whammy – sluggish growth, inflation, and high borrowing costs – took a toll on businesses worldwide. Therefore, it came as no surprise that the IMF's Q4 2023 economic outlook projected global growth would dip from 2022's 3.5% to 3.0% in both 2023 and 2024.[4]

INNOVATIONS AND ADVANCEMENTS

Technological advancements and industry trends like generative AI, open banking, cloud and edge computing, and ESG data hubs have the potential to reshape banking operations by meeting the changing expectations of customers in an increasingly fast-paced, technology-driven world.

- As generative AI use cases proliferate, banks will likely build capability-enhancing solutions – first for internal efficiency and then, over time, for a better customer experience.[5]
- Open banking is empowering customers and enabling banks to innovate in providing products and services tailored to user's financial data.
- Amid heavy reliance on digital infrastructure and technology for essential services, banks will need to prioritize investing in digital operational resilience to ensure uninterrupted financial services, data protection, and regulatory compliance.
- Banks are targeting affluent customers by providing tailored products and services with a focus on engaging and retaining this valuable segment.

LOOKING BACK AT 2023

Let's recap last year's trends. A year ago, we highlighted the increasing global focus on sustainability, and indeed, ESG data has emerged as an essential driver for bank executives' business decisions. We also anticipated bank caution around decentralized finance use cases, and reluctance continues to prevail, although 2024 regulations may boost sector confidence. Cloud migration also continues to deliver value for banks, with many opting for a hybrid approach.

THE YEAR AHEAD

In 2024, despite ongoing challenges, inflation should continue to fall. If brought under control, lower interest rates and a potentially smoother path forward await the banking industry. Until then, however, financial institutions must demonstrate resilience and focus on both deposit retention and growth in a very competitive landscape. Lending also remains complex, with high borrowing costs and anticipated declines in credit quality and collateral values. Enhancing operational resilience will be crucial to ensuring customers receive secure, uninterrupted services that strengthen their confidence and loyalty.

TOP TRENDS FOR 2024

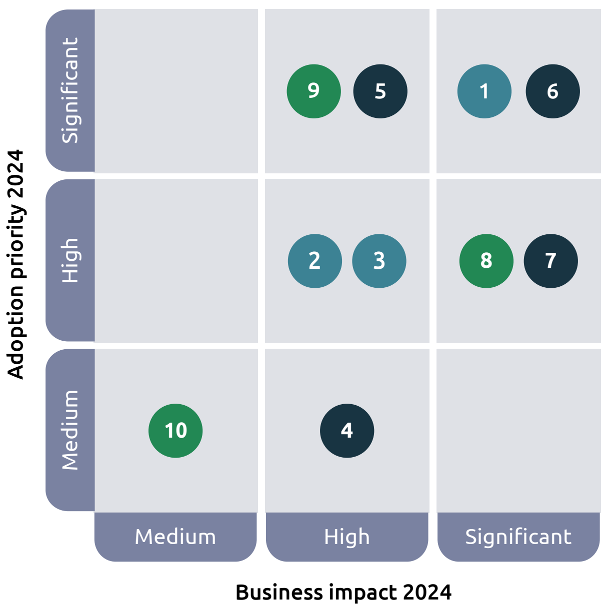
We based our 2024 retail banking trends on analysis across three broad themes:

- **Customer first:** Examines the impact of a rapidly changing market and how banks are adopting strategic measures in response to shifting customer behaviors and demands.
- **Enterprise management:** Delves into organizational priorities for banks to manage risks, embrace digital solutions, and streamline operations.
- **Intelligent industry:** Explores how banks can leverage new technologies and adapt to evolving regulations to derive benefits across the value chain.

RETAIL BANKING TOP TRENDS 2024 - PRIORITY MATRIX

Customer first | Enterprise management | Intelligent industry

1. Banks compete for customer deposits as they navigate through business turbulence
2. New-age players are switching gears from hyper-growth to profits
3. Banks pamper affluent customers with personalized products and services
4. Banks expand ESG data use beyond compliance to strategic decision-making
5. Digital operational resilience is a top priority as cybersecurity threats increase
6. Cost control is necessary to hedge against economic volatility
7. The next wave of innovation in cloud lies in edge computing, sovereign cloud, and cloud marketplaces
8. Banks explore generative AI to elevate productivity
9. Data is evolving from a proprietary asset to a shared, open resource
10. Decentralized finance continues to evolve; banks need to be ready for soon-to-come regulatory frameworks



Source: Capgemini Research Institute for Financial Services analysis, 2023

The priority matrix above presents Capgemini's 2024 trend prioritization in an operating environment that includes:

- Softening inflation and high-interest rates, coupled with stagflation trends
- Geopolitical instability
- Dynamic regulatory activity
- Intense competition and increased focus on customer centricity due to the impact of new-age players
- Operational cost overruns and high capital lock-in

Adoption priority – The criticality of adopting a 2024 trend to maximize value creation because of its sector importance.

Business impact – The effects of a trend on the sector's 2024 business as it relates to customer experience, operational excellence, regulatory compliance, or profitability.

Circumstances will vary for each firm depending on business priorities, geographic location, and other factors. For more information, don't hesitate to contact us at banking@capgemini.com.

FROM 2023 TO 2024, WHAT HAS CHANGED AND WHAT HAS NOT?

	TRENDS 2024		TRENDS 2023
1	Banks compete for customer deposits as they navigate through business turbulence	1	Smart branches feature experiential banking and convenience to spark customer connection
2	New-age players switching gears from hyper-growth to profits	2	Incumbents scout for mature FinTechs to complement capabilities, boost bank profitability
3	Banks pamper affluent customers with personalized products and services	3	More banks commit to driving circular economy sustainability
4	Banks expand ESG data use beyond compliance to strategic decision-making	4	Banks step up and own customer experience with embedded finance
5	Digital operational resilience is a top priority as cybersecurity threats increase	5	Financial wellness advice can help customers navigate the cost-of-living challenges
6	Cost control is necessary to hedge against economic volatility	6	CMOs leverage actionable data insights to guide customer centricity
7	The next wave of innovation in cloud lies in edge computing, sovereign cloud, and cloud marketplaces	7	Digital identity to unlock efficiency gains for banks
8	Banks explore generative AI to elevate productivity	8	Banks unlock value at scale by migrating workload to the cloud
9	Data is evolving from a proprietary asset to a shared, open resource	9	A boom in synthetic data will catalyze data ecosystem growth
10	Decentralized finance continues to evolve; banks need to be ready for soon-to-come regulatory frameworks	10	As banks explore decentralized finance, they remain cautious

New trends	Trends evolution	Deprioritized trends
• In the face of challenging macroeconomic conditions, banks are vying for customer deposits and focusing on being lean while navigating through a turbulent landscape marked by high interest rates. • Open banking, driven by the democratization of data, and generative AI are deeply impacting the banking industry amid customerdemand for increasingly innovative products and tailored services.	• Defined standards for ESG data are enabling banks to leverage it increasingly to unlock strategic value for their business. • Cloud computing combined with edge devices can balance faster processing, data sovereignty, and cost savings. • Decentralized finance has seen muted activity, but regulations in 2024 could give a boost to the sector.	• Instead of full-fledged smart branches, new cost-effective formats such as shared banking hubs have emerged. • Although well-capitalized incumbents still have an opportunity to acquire FinTechs, more M&A activity has been seen among struggling regional banks. • Banks continue to invest in embedded finance, digital identity, and synthetic data, but prevailing economic conditions have brought forth more urgent challenges.

Source: Capgemini Research Institute for Financial Services analysis, 2023.

TREND 1

Banks compete for customer deposits as they navigate through business turbulence

In the aftermath of record outflows, bank deposit strength is crucial for crisis prevention and long-term resilience, especially for US regional banks.

CONTEXT

The 2023 collapse of five regional US banks (Silicon Valley, Signature, First Republic, Heartland Tri-State, and Citizens) and the government lifeline tossed to Switzerland's Credit Suisse cast a worrisome cloud over the financial sector.[6, 7] US regional banks experienced a sharp stock price decline, primarily due to concerns about potential deposit outflows, which could lead to capital challenges for other regional banks.[8] Globally, high interest rates led to substantial outflows from traditional savings accounts.

- Data from the US Federal Deposit Insurance Corp (FDIC) revealed the most significant quarterly decrease in deposits since records began in 1984, with a reduction of USD 472.1 billion, or nearly 3%, in the first quarter of 2023. Over four consecutive quarters, deposits spiraled down.[9]
- Total deposits fell in several major European markets in early 2023. According to data from S&P Global Market Intelligence and the European Central Bank (ECB), deposits at monetary financial institutions in France, Italy, Spain, the Benelux region, and the Nordic region were lower in March 2023 compared with March 2022, with Spain showing the largest decline at 5.9%.[10]
- British households withdrew money from their savings in May 2023 at a record pace as rising interest rates slowed borrowing, according to Bank of England data. Households drained a net GBP 3.8 billion (USD 4.6 billion) from savings – the most significant outflow since recordkeeping started 25 years ago.[11]

CATALYSTS

In the aftermath of prominent bank failures, regulatory oversight of US regional banks intensified. Meanwhile, customers worldwide have been demanding higher interest rates, withdrawing deposits, and seeking enhanced security.

- In response, US regulators are forcing regional banks to bolster their liquidity planning. The Federal Reserve privately cautioned multiple lenders with assets ranging from USD 100 billion to USD 250 billion as part of an intensified supervisory initiative. Notable recipients of these warnings included Fifth Third Bancorp and M&T Bank Corp. The notices cover capital, liquidity, technology, and compliance.[12]
- Tech firms and apps are offering customers attractive rates. Apple launched a high-yield savings account with Goldman Sachs in April 2023, offering an annual percentage rate of 4.15% – more than 10 times the national average. This product generated almost USD 1 billion in deposits within four days of launch, and USD 10 billion between April and August.[13, 14] Online discount brokerage Robinhood also raised savings account rates, to a yield of 4.65% annually.[15]
- Deposits in the United States shifted to money market funds in the first half of 2023, the Bank for International Settlements (BIS) reported in Q3 2023.[16] This trend continued into the third quarter, as money market funds attracted USD 184 billion in net inflows during the period.[17]

IN A NUTSHELL

Banks are competing for customer deposits by offering higher interest rates, account sign-up bonuses, and various other strategies to counter outflows.

- More than a dozen US lenders, including Capital One, were offering a 5% annual percentage yield on one-year CDs in Q1 2023, which might have been unthinkably high two years prior. Even banking giants like Wells Fargo offered 4% on 11-month CDs.[18]
- As of November 2023, the average savings account rate across all financial institutions in the US was 0.45%, according to the FDIC, more than double the rate around the same time in the prior year, which stood at 0.21%.[19] An increasing number

of banks are providing higher savings account rates, such as Capital One at 4.3%, Ally Bank at 4.25%, and Lending Club offering 4.5% in the US.[20] European banks also started offering higher rates, including Germany's Deutsche Kreditbank increasing rates to 3.5%, Santander offering 5.2% in the UK, and Italy's UniCredit offering 6.7% for customers who keep their deposits with the bank for more than a year.[21]

- US banks are doubling down on offering signing bonuses for opening new accounts or making regular deposits. Capital One offered a USD 100 bonus for opening a new savings account and maintaining balances over USD 10,000 for 90 days, with the incentive increasing to USD 1,000 for deposits exceeding USD 100,000. Discover Financial Services and LendingClub were providing similar offers.[22]
- Innovative regional bank strategies to retain deposits include educating customers about deposit insurance regulations, introducing diverse product offerings, and highlighting bank connections to local communities. Bankers are also advising clients to add household members to accounts to maximize available insurance coverage. In addition, mid-sized banks are introducing bank-insured cash sweeps for businesses that allow a bank to allocate a company's deposits among fellow banks, ensuring a more significant portion of its cash flow is covered.[23]

Figure 1: Increasing deposits is crucial for resilience in the banking sector

Five successive quarters of outflows	Deposit outflows were prevalent for five successive quarters since Q2 2022, and were accelerated by the failure of three U.S. banks–Silicon Valley, Signature, First Republic.
Higher cost of deposits	High interest rates have increased funding costs, and deposit costs have risen more sharply for regional banks as compared to incumbents as they started offering higher rates to attract more deposits.
Higher interest rates and offerings to attract depositors	Apart from higher interest rates on savings accounts and certificates of deposit, banks also started offering signing bonuses for new accounts and regular deposits.
Opportunities for M&A	The Fed has navigated bank collapses by encouraging the acquisition of smaller, struggling banks by larger incumbents; regional banks could also merge to shore up depositors' confidence and stabilize their deposits.

Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

Deposits are traditionally sticky: changing banks can be a hassle, and depositors tend to be slow to move their funds even if they could earn a higher interest rate elsewhere. However, amid several quarters of deposit outflows, the collapse of three US regional banks triggered record withdrawals at several regional banks in Q1 2023.

As rates rose, high-yield savings accounts became fashionable once again, with regional banks competing aggressively to stay at the top of the rate tables that consumers rely on for comparison purposes. However, the higher cost of deposits could potentially impact the bottom line for these banks. The trend in 2024 will continue to be deposit growth for regional banks. It is also crucial to rebuild investor confidence.

Deposits at European-headquartered banks have been more stable, with the Credit Suisse failure being an isolated incident; the spread between deposit rates and interest rates is lower, helping prevent mass deposit outflows. However, increased competition and a shift to longer-term deposits could increase funding costs, leading to reduced profitability.

The US Federal Reserve navigated the regional banking crisis by encouraging the acquisition of smaller, struggling banks by more established firms, as seen when J.P. Morgan acquired First Republic Bank.[24] The trend may continue in 2024 and beyond, and regional banks could also consolidate among themselves to rebuild depositors' confidence and stabilize deposits.

TREND 2

New-age players are switching gears from hyper-growth to profits

Neobanks and challengers are working to meet revenue challenges through deeper customer engagement, product diversity, and new business models.

CONTEXT

From their financial services beginnings (almost a decade ago in Europe), new-age players* generated venture capital buzz while attracting tech-savvy, convenience-minded customers. Newcomer innovations and agile digital-first approaches upended conventional physical-branch paradigms to catalyze banking competition industrywide.

- Global consultancy Simon-Kucher reported that worldwide neobank customers surpassed ~1.1 billion in July 2023 – growing 31% over January 2022, with revenues increasing by 43% to reach USD 83 billion.[25]
- Initially, most new-age players adopted a growth-first approach, with financial success taking a back seat. Of around 400 neobanks with a collective one billion customer accounts globally, fewer than 5% were profitable in 2022.[26]

CATALYSTS

Banking newcomers continue to attract new customers, but the world economy has slowed funding, which makes it challenging to sustain expansion ambitions. However, some large new-age banks have begun to rack up profits, potentially paving the path for others.

- More than two-thirds (67%) of participants in Capgemini's World Retail Banking Report 2022 consumer survey said they use the services of new-age players, including neobanks, challengers, and digital banks.[27] Additionally, more than 75% of respondents said fast, low-cost services that are accessible and easy to use motivate them to consider switching to a FinTech provider.[28]
- Venture capital flows into FinTech firms dropped globally by 36% year over year, down to USD 6 billion in Q3 2023.[29]
- After achieving its first full year of profits in 2022, Starling Bank, a UK-based challenger, reported a sixfold increase in pre-tax profits to reach GBP 195 million (over USD 242 million) in 2023.[30, 31] London's digital-only bank Revolut recorded its first full year of profit in 2021.[32] Revolut is active in the United States with a banking-as-a-service (BaaS) arrangement and opened a Manhattan headquarters in Q4 2023. Brazilian Nubank, South Korea's Kakao Bank, and UK-based foreign exchange FinTech Wise accomplished positive earnings in 2023, according to Simon-Kucher.[33]

IN A NUTSHELL

New-age players are strategically diversifying offerings (particularly credit products) to meet customer needs more profitably. Still focused on convenience and customer experience, they are also looking beyond financial services to engage customers in their daily lives. Moreover, they are exploring sustainable business models based on disciplined costs, partnerships, and measured expansion. Well-capitalized firms are also strategically acquiring peers with complementary capabilities.

- Nubank launched personal loans in Mexico in September 2023 with a fully digital application process that takes less than five minutes. To bolster its Mexican presence, Nubank has expanded beyond credit cards to offer a suite of financial services including savings accounts, debit cards, and now, loans.[34] In its native Brazil, Nubank launched Nucoin, a free crypto token that rewards user engagement through a loyalty program.[35]

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*New-age player: A digital-first firm that offers financial services. The list of new-age players includes (but is not limited to) neobanks, challenger banks, or digital banks operated by industry incumbents.

- German digital bank N26 launched a cryptocurrency trading product that lets customers buy and sell almost 200 cryptocurrencies through their mobile app.[36]
- Revolut launched an in-app marketplace allowing customers to book their travel experiences directly, offering up to 10% cash back and zero booking fees.[37] Swedish FinTech Klarna introduced a suite of non-financial new features, including Shopping Lens, an AI-powered image-search tool. The company is also launching shoppable videos in Europe, in-store product scanning, a new cash-back program, express refunds, and more.[38]
- In the United States, FinTech Greenwood, which provides banking services to black and latinx communities, acquired the mobile banking platform Kinly. The acquisition merges two organizations with a mission to help underserved communities build generational wealth.[39]
- Dutch neobank Bunq acquired Belgian FinTech TriCount, an expense-sharing specialist, in 2022 to add 5.4 million new users.[40]

Figure 2: The path to profitability for new-age digital banks

Launch Phase

Emphasize targeted marketing for customer acquisition. Most focus on a limited number of core offerings and providing convenient, frictionless digital experiences.

Growth Phase

Prioritize increasing the customer base through strategic geographical and product portfolio expansions, while simultaneously contending with regulatory requirements.

Profitability Phase

Monetize through cross-selling higher-margin products, form ecosystem partnerships, and prioritize brand loyalty to foster lasting relationships.

Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

It was the promise of personalized customer experience and low fees that initially drew users to new-age digital banks. However, today's volatile macroeconomics and closures of financial institutions amplify concerns about trust and security. As incumbent banks invest more in apps and digital services, new-age players will likely ramp up innovation to remain competitive in 2024 and beyond.

Amid lower funding and increasing competition, expect new-age players to recalibrate growth ambitions and prioritize profits. We anticipate increased diversification to cross-sell higher-margin products to existing customers. Further, challenger banks will move beyond financial services to engage customers more comprehensively through lifestyle-related services. Consequently, we foresee more super apps emerging from new-age banks and FinTechs as they vie to become the primary bank for their customers.

TREND 3

Banks pamper affluent customers with personalized products and services

Banks are ramping up efforts to cater to affluent customers, developing products and services tailored to their specific needs and crafting premium experiences to secure long-term loyalty.

CONTEXT

In pursuing the next growth phase, banks are strategically increasing their focus on the burgeoning affluent class, recognizing the immense opportunity within this demographic and their future wealth potential.

- According to the Capgemini World Wealth Report 2023, the affluent wealth band – with investable assets of USD 250,000 to USD 1 million – holds nearly USD 27 trillion in wealth and represents a significant population base, outnumbering the HNWI* segment by 2.5 times.[41]
- Further, 71% of affluents surveyed for the report revealed that they would like wealth management services from their retail banks.[42]

CATALYSTS

Consumers say they want more personalized banking experiences, and cost-of-living anxieties are amplifying customers' need for financial advice.

- According to survey results from the Capgemini World Retail Banking Report 2022, 44% of customers said banking is not personalized, while 52% said banking is not fun.[43]
- And almost two-thirds (64%) of retail banking executives identified personalized offerings based on internal and external data to be one of the most striking innovations.[44]
- Customer financial health declined nine percentage points year over year in 2023, according to the J.D. Power 2023 U.S. Retail Banking Satisfaction Study SM. For the survey, customer financial health is measured as a metric encompassing spending/savings ratios, creditworthiness, and safety net items like insurance coverage. While only 21% of consumers said they received advice or guidance during the past year, nearly half (47%) of individuals who received advice opened a new account, the survey found.[45]

IN A NUTSHELL

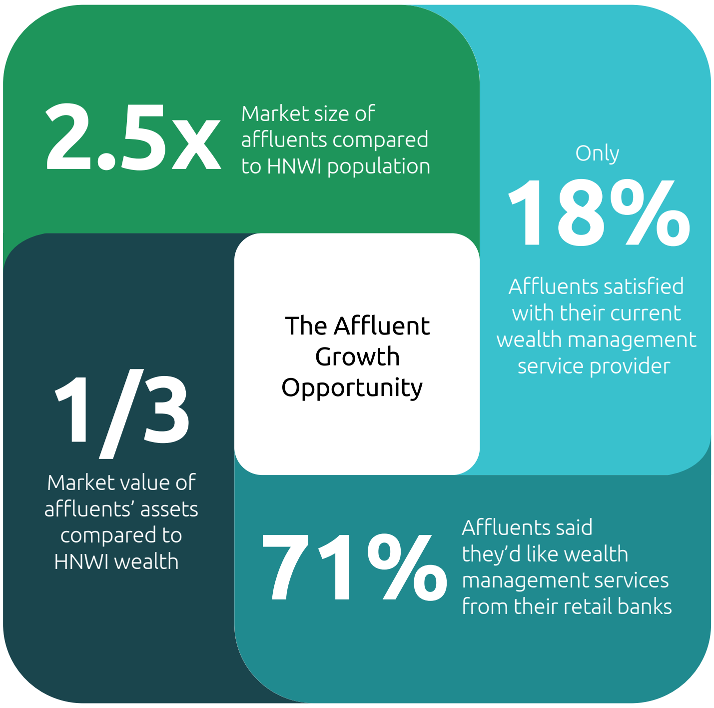
In an effort to attract affluent customers, retail banks are providing exclusive benefits and personalized experiences. To enable catering to this segment in a profitable manner, we are observing a convergence in core banking, lending solutions, and wealth management to help meet the diverse and evolving needs of affluent customers.

- In September 2022, Standard Chartered Bank launched a new deposit account in Singapore, Wealth $aver, that offers higher interest rates for wealthy clients based on their total existing assets under management, including total deposits, investments, and insurance products held with the bank.[46]
- Citi introduced a new set of relationship tiers in August 2023 based on average monthly balances. Higher tiers equate to more benefits and services, including waived service fees on checking and savings accounts, waived Citi fees at non-Citi ATMs, and professional financial planning.[47]
- In January 2023, Société Générale completed the merger of its two French retail banking networks, Société Générale and Crédit du Nord Group to launch SG, the Group's new French retail bank. SG aims to be an expertise bank with offerings personalized to the needs of different customer segments – including the setting up of a wealth bank and a single advisor for business customers, both for their personal and professional needs.[48]

*High net-worth individuals (HNWIs) have investable assets of USD 1 million or more, excluding primary residence, collectibles, consumables, and consumer durables.

- In 2022, Bank of America created a group that caters to wealthy clients. It underwrites margin loans, securities lending, mortgages, and vehicle loans while working alongside financial advisers and private bankers, who continue to handle investments. The bank's wealth and consumer units run the group.[49]
- Citigroup created Citi Alliance to sell products through independent advisers. It offers core banking and lending solutions to independent advisers and broker-dealers.[50] In 2024, wealth management firm Edward Jones will leverage the platform to provide banking services like checking and savings accounts.[51]
- After taking over First Republic Bank, J.P. Morgan said it would upgrade FRB branches to appeal to high-wealth customers.[52] In Hong Kong, Standard Chartered plans to open three more outlets aimed at wealthy clients.[53]
- In early 2023, Wells Fargo launched LifeSync, a digital platform for prosperous clients. The platform helps investors manage and track their financial goals, net worth, portfolio performance, market indices, and credit card reward balances.[54]

Figure 3: The growing affluent segment presents a lucrative opportunity for banks



Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

Recognizing the substantial wealth potential within the affluent demographic, banks are placing bets on their future financial growth. By tailoring products and services and crafting premium experiences, institutions are establishing early relationships with these customers in a bid to secure their long-term loyalty. This forward-looking approach acknowledges that today's affluent customers may amass even greater wealth as their financial journey progresses.

Retail banks are offering better rates and waived fees, a higher degree of personalization, and value-added services such as financial planning, to build long-term relationships with affluent customers. Moreover, banks that engage early with these individuals create life cycle cross-selling opportunities. Banks that seamlessly integrate banking and other services, such as wealth management, can capitalize on synergies as affluent customers expand their wealth.

TREND 4

Banks expand ESG data use beyond compliance to strategic decision-making

Initially sparked by regulatory mandates, banks are evolving their ESG strategies as business growth drivers.

CONTEXT

Environmental, social, and governance (ESG) data has become highly sought after by investors, regulators, and consumers. Although once driven by regulations and disclosure requirements, these days, banks are baking ESG considerations into their business strategy as competitive and market growth imperatives.

- From 2019 to 2023, products featuring ESG-related claims grew by 28%, surpassing those that did not prioritize ESG factors, with an average 20% growth rate, according to a 2023 McKinsey/Nielsen study.[55]
- Diverse performance illustrates the growing importance of ESG considerations for consumers and investors. As a result, retail banks are weaving sustainability into product offerings and strategic planning.

CATALYSTS

The Capgemini Research Institute for Financial Services' PoV report, "Wealth managers can reignite investors' waning ESG enthusiasm" highlighted that significant and ever-increasing numbers of HNWIs are asking for reliable, traceable ESG data.[56] In an era of heightened environmental consciousness, the financial services industry is witnessing a surge of initiatives and platforms dedicated to sustainable banking and investments.

- As of September 2023, the UN-convened Net-Zero Banking Alliance included 133 members worldwide, with more than half in Europe. The alliance brings together banks committed to aligning their operations to reach net-zero emissions by 2050. Each bank's CEO must sign a commitment statement to enter the coalition. Along with the 2050 target, the agreement binds the bank to set an emission target for 2030 and intermediary targets every five years.[57]
- Nasdaq launched ESG Data Hub, connecting investors with sustainability data sets from leading providers across various environmental, social, and governance categories.[58]
- J.P. Morgan introduced Sustainable Investment Data Solutions for institutional investors, enabling investors to access sustainable investment data supplied by providers and various analysis tools.[59]
- According to a report from the Morgan Stanley Institute for Sustainable Investing, in the first half of 2023, sustainable funds provided a median return of 6.9%, beating the 3.8% of traditional funds. Investor demand also remained strong as sustainable funds' assets under management (AUM) reached record levels.[60]
- Restriction screening, which investors use to vet products or activities based on their values or regulatory requirements, has risen sharply. More than 20% of total global assets under management underwent at least one restriction screen in 2023, a surge from 2% in 2019.[61]

IN A NUTSHELL

Many banks are innovating to develop green products, services, and experiences along the customer lifecycle, engaging through environmentally friendly offerings.

- Barclays, Citibank, and HSBC provide carbon financing and emissions trading services. Meanwhile, CaixaBank extends sustainability-linked loans, and ABN AMRO specializes in green technology leasing. In addition, Singapore-based OCBC Bank and HSBC facilitate green SME financing and support, with BBVA and multinational Spain-based CaixaBank offering financing options for sustainable agriculture. BBVA also includes green pension plans among its offerings for retail customers.[62]
- In 2022, First Abu Dhabi Bank, the UAE's largest bank, launched a sustainability-linked current account for corporate clients.[63]
- Barclays' Green Home Buy-to-Let Mortgage debuted in 2022, rewarding landlords who buy an energy-efficient new home with lower interest rates on their mortgage.[64]

- Commonwealth Bank of Australia provides personalized carbon footprints for customers based on their spending data, allowing retail customers to view their carbon footprint via an app and offset their transactions by purchasing carbon credits.[65]
- DBS Bank's gamified metaverse experience, BetterWorld, educates users about global sustainability challenges and sustainable lifestyle best practices. The virtual experience highlights the global food waste challenge and supportive DBS initiatives.[66]

Figure 4: Four strategic areas to leverage ESG data

Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

ESG considerations are no longer confined to regulatory mandates but are now integral to business strategy. Further, the growing interest of Gen Z and millennials in ESG initiatives is compelling banks to integrate ESG considerations into every decision-making process. ESG data hubs are becoming pivotal in democratizing sustainability information access. Transparency regarding ESG initiatives empowers stakeholders, from investors to consumers, with critical insights into a bank's sustainability performance. Further, ESG data is pivotal for developing and pricing green products and services.

We anticipate that retail banks' focused commitment to sustainability will be a competitive advantage in the years ahead. ESG considerations positively correlate with financial performance and customer appeal, enabling banks to expand portfolios of environmentally friendly products and services. Banks that transparently support ESG principles can attract eco-conscious consumers and businesses and bolster trust and loyalty.

TREND 5

Digital operational resilience is a top priority as cybersecurity threats increase

As businesses and society become increasingly dependent on digital technologies and processes, the impact of digital disruptions has grown significantly.

CONTEXT

In a time when financial institutions rely heavily on digital infrastructure, data, and technology to deliver essential services and maintain customer trust, frontrunners are prioritizing digital operational resilience to ensure uninterrupted financial services, protect sensitive customer information, and comply with government regulations.

- A 2022 Juniper Research study predicted that enterprise cybersecurity spending will exceed USD 226 billion in 2027, up from USD 179 billion in 2022. This growth, of 26% over five years, reflects a maturing cybersecurity market which continues to evolve as new threats emerge.[67]
- The Swedish financial regulatory authority imposed a substantial fine on Swedbank, citing inadequate internal controls. Swedbank experienced a significant IT disruption in April 2022. Similar incidents have affected other banks, including DBS and Citibank, leading to customer inconvenience and significant fines from regulators.[68]

CATALYSTS

Operational resilience is necessary for technology businesses, particularly for those in highly regulated industries that process financial information including banks, payment processors, or insurance companies. It is instrumental in bolstering banks' anti-money laundering (AML) efforts. Through technology investments and enhanced data analytics, banks can improve AML monitoring and detection.

- 84% of the more than 120 global cyber decision-makers who participated in a 2022 World Economic Forum survey said cyber resilience is a business priority in their organization, with support and direction from top leadership.[69]
- In November 2022, the European Union published the Digital Operational Resilience Act (DORA) to add information and communications technology (ICT) requirements to previous operational resilience regulations for financial services providers in EU member states.[70]
- In March 2021, a notable development in regulatory approach occurred when NatWest Bank faced a GBP 264.8 million (USD 322 million) fine for inadequate monitoring of a high-risk customer under the UK's Money Laundering Regulations. In the same period, HSBC received a GBP 63.9 million (USD 78 million) fine for ineffective transaction monitoring systems.[71]

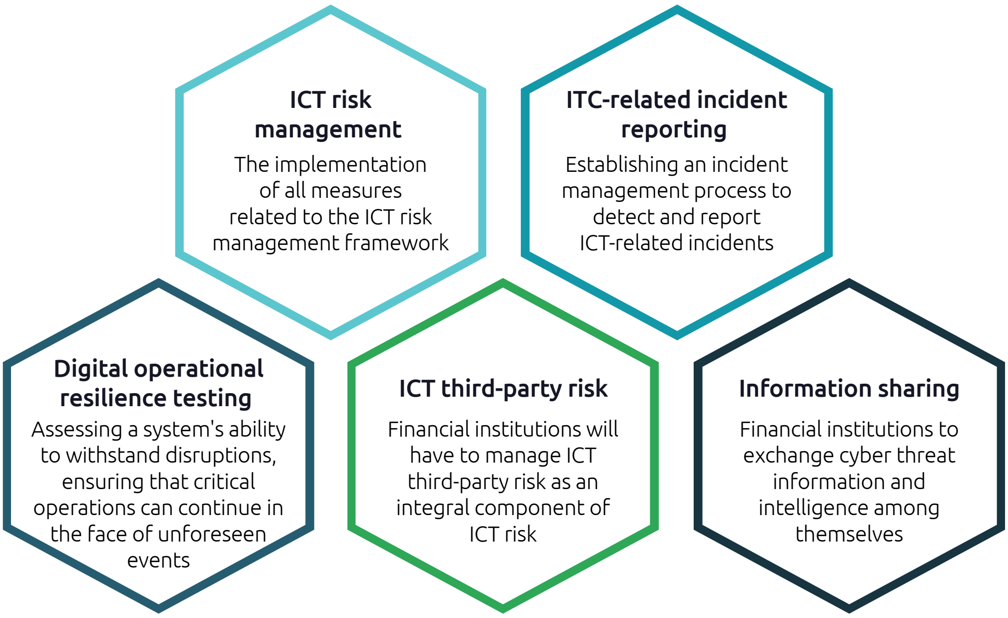
IN A NUTSHELL

Advances in technology – including the proliferation of cloud computing, big data analytics, artificial intelligence, and cybersecurity tools – are some of the key tools being leveraged by organizations to enhance their security capabilities. The need to protect against cyber threats is a significant driver of resilience-related investments.

- Bank of America increased tech spending in 2023 to USD 3.7 billion from USD 3.4 billion in the prior year, or 9% growth. The company may reduce headcount due to macroeconomic challenges but will retain robust tech spending.[67]
- Commonwealth Bank of Australia's (CBA) cyber team leverages AI to boost its safety capabilities as online cybercrime increases exponentially.[68] CBA estimated its 2022 Information and Communication Technologies (ICT) budget at AUD 1.6 billion (USD 1 billion); CBA earmarked a significant portion for software, ICT services, and vendor hardware.[69]

- ING, a leading Dutch banking company, and Quantexa, a global decision intelligence leader, partnered to strengthen ING's operations. The partnership seeks to bolster ING's risk detection and investigation capabilities with Quantexa's Decision Intelligence Platform.[75]
- In July 2023, BBVA, the Spanish multinational bank, announced the launch of a unit dedicated to strengthening the bank's financial crime prevention unit, comprised of 800 employees.[76]

Figure 5. Five pillars of digital operational resilience



Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

Digital operational resilience holds particular significance for banks due to the financial sector's high dependence on digital technology and data; its impact on banks includes ensuring uninterrupted financial services, protecting customer data, and complying with stringent regulatory requirements. Investment in operational resilience safeguards a bank's financial stability, reputation, and the trust of its customers. It mitigates risks associated with cybersecurity threats, system failures, and regulatory non-compliance.

Additionally, robust operational resilience enhances a bank's competitive position, allowing it to recover quickly from disruptions, minimize losses, and gain a strategic edge in the market. In an evolving financial landscape, the impact of digital operational resilience is pivotal for banks seeking to navigate uncertainties and maintain the trust and confidence of customers and regulators.

TREND 6

Cost control is necessary to hedge against economic volatility

Banks are prioritizing cost control and lean budgets as they face uncertain macroeconomic conditions and a global slowdown.

CONTEXT

Cost-of-living increases, rising interest rates, and geopolitical upheavals are rocking the global economy and retail banks everywhere. In addition to large-scale digital transformation projects to improve efficiency and save costs, banks have also been trimming their networks of physical locations for many years now.

- The International Monetary Fund projects global real GDP growth to fall from an estimated 3.5% in 2022 to 3.0% in 2023 and 2024.[77]
- Banks have been closing their branches at a rapid pace, which was further accelerated by the Covid-19 pandemic. In the US, there were nearly 100,000 branches in 2009, which declined to fewer than 80,000 in 2023, according to S&P Global Market Intelligence data.[78] Similarly in the UK, almost three-fifths of bank branches have been shuttered since 2015 according to analysis by the Financial Times.[79]

CATALYSTS

High-profile 2023 bank failures surprised the world, and regulators responded with increased scrutiny. Now, banks are under pressure as they navigate an uncertain macroeconomic environment amid recession fears: not surprisingly, they are cautiously reducing costs.

- After the sudden failures of Silicon Valley Bank and Signature Bank, regulators are likely to tighten oversight on mid-sized institutions, particularly those in the USD 100 billion to USD 250 billion asset range.[80]
- Banks have not yet experienced the full effects of inflation on their operating expenses due to a combination of fixed-price contracts and a delay in cost increases, particularly in areas like salaries. Globally, wages are increasing by approximately 5% to 10%, indicating that operating expenses may see high single-digit increases, according to Kearney's 2023 European Retail Banking Radar.[81]
- US banks are allocating larger provisions to prepare for potential loan losses, indicating a widespread acknowledgment of possible credit deterioration. According to S&P Global Market Intelligence, almost two-thirds of the 25 financial institutions analyzed (each with at least USD 10 billion in assets) have seen sequential increases in loan loss provisions (LLPs).[82]
- In the eurozone, loan demand from businesses fell to its lowest since 2003, while in the United States lenders experienced similarly weak loan demand from businesses and consumers amid high interest rates.[83, 84] With pressure on the bottom line and margins of banks, they are likely to cut costs.

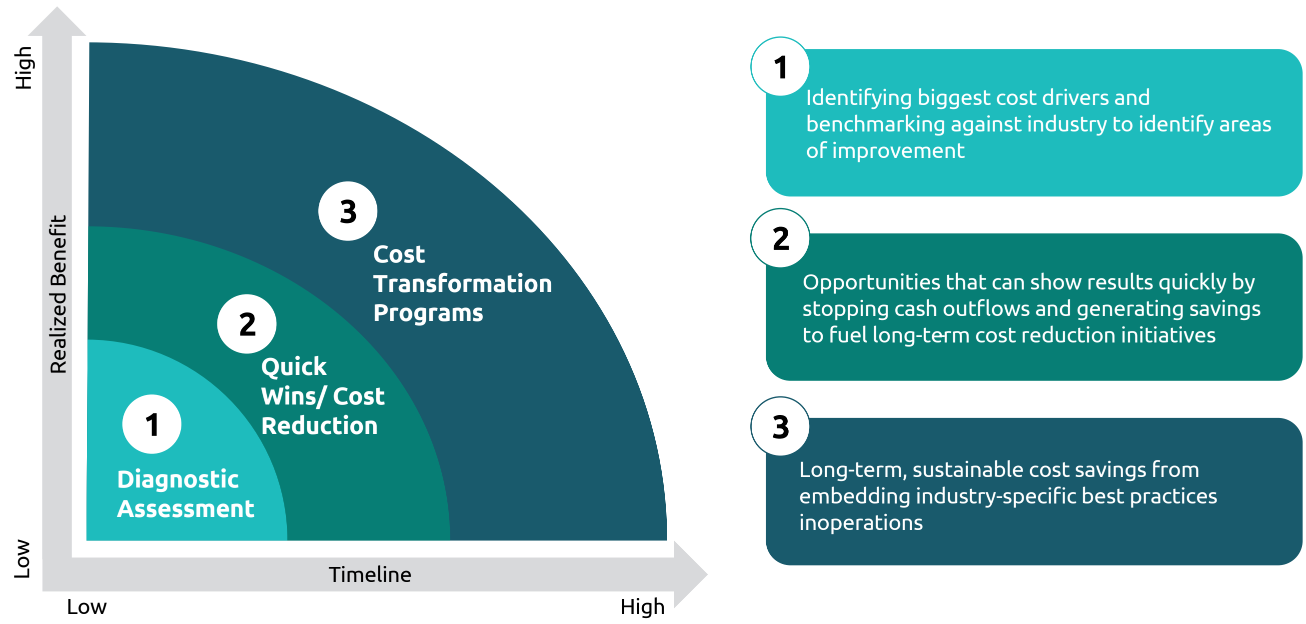
IN A NUTSHELL

Apart from cost-cutting measures such as staff reductions, initiatives have also catalyzed innovation, and banks have continued to focus on leveraging technology to automate processes and reduce operating costs.

- Goldman Sachs, Morgan Stanley, J.P. Morgan Chase, Citigroup, and Wells Fargo announced or warned about layoffs in 2023 as part of cost-cutting to weather the uncertain economic climate.[85]
- Across the UK, seven shared banking hubs have started operations, with more than 60 planned. Funded by the banks and designed to offer basic banking services for communities without traditional branches, the hubs are shared bank branches with each facility housing multiple banks' representatives.[86]
- Australian banks are automating the loan process and cutting overhead such as staffing and real estate: Commonwealth Bank of Australia launched a fully digitized loan service that processes applications in 10 minutes. ANZ, National Australia Bank, and Westpac plan automation initiatives with an emphasis on cost reduction.[87]

- BNP Paribas exited the highly competitive US retail banking market after the sale of its subsidiary, Bank of the West, to BMO Financial Group, a Canadian bank.[88]
- In 2019, Deutsche Bank announced a cost reduction program aimed at lowering its cost/income ratio. By 2022, they had successfully reduced it to 75%, down from 85% in 2021. They have reaffirmed their commitment to further decrease the ratio to 62.5% by 2025.[89]
- After taking over Credit Suisse, UBS announced a plan to cut costs by USD 10 billion by the end of 2026.[90]
- Banks are tightening lending standards, anticipating declines in loan portfolio credit quality and customer collateral values. This adjustment also stems from a decrease in risk tolerance, along with concerns regarding bank funding costs, liquidity position, and potential deposit outflows.[91]
- In the second quarter of 2023, most banks have reinforced their lending criteria, with plans to continue this trend due to economic concerns. According to the Senior Loan Officer Opinion Survey administered by the Federal Reserve, a growing number of banks have tightened their lending standards across various credit categories, including business loans, mortgages, car loans, and commercial real estate loans.[92]

Figure 6. Three-horizon approach for cost reduction



Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

Amid global economic uncertainties, banks are streamlining operations and cutting excesses. Higher deposit costs, coupled with slowing loan demand, are exerting pressure both on income and profit for banks, further highlighting the need to control costs. This cautious approach will likely persist throughout 2024 or until macroeconomic conditions improve.

As banks have continued to rationalize their networks by closing down branches and ATMs, these challenges have also catalyzed innovation as new formats, such as shared banking hubs, have emerged. While banks may be reducing overall staff, they are likely to invest in talent in key areas like AI, cybersecurity, and cloud. Moving forward, banks will continue to focus on digital infrastructure improvements and leveraging technology to automate processes and reduce operating costs.

TREND 7

The next wave of innovation in cloud lies in edge computing, sovereign cloud, and cloud marketplaces

Innovations in cloud will empower banks to establish an efficient technology infrastructure, leading to a balance between faster data processing, data sovereignty, and cost savings.

CONTEXT

The Capgemini World Cloud Report 2023 – Financial Services revealed that more than 90% of banking firms have initiated their cloud journey, but most are still not cloud-native.[93] As banks continue their migration to the cloud, technologies such as edge computing, sovereign cloud, and cloud marketplaces can enable them to derive enhanced value from this transition.

- Edge computing is a distributed computing paradigm that brings data processing and computation closer to the data source, or the edge of a network; it is different from the traditional model of centralizing computing in data centers or the cloud. Market research firm IDC says global spending on edge computing will have reached USD 208 billion in 2023, more than 13% higher than in 2022. Expenditure by enterprises and service providers on hardware, software, and services for edge solutions will maintain its growth trajectory, and by 2026, spending may likely surge to roughly USD 317 billion.[94]
- Amid heightened concerns about data sovereignty, a sovereign cloud keeps data within the specific country or region it belongs to, making sure it never crosses borders and always stays within one jurisdiction. The European Union is considering a proposal mandating cloud providers to store their data exclusively within the zone to be eligible for the highest cybersecurity certification, aiming to safeguard EU data from potential interference by foreign governments.[95]
- A cloud marketplace is a centralized platform that allows users to browse, discover, and purchase cloud computing services and products from different independent vendors. Market analyst firm Canalys projects that by 2025, cloud marketplaces will grow to more than USD 45 billion, representing an 84% CAGR from 2020.[96]

CATALYSTS

The increasing accessibility of infrastructure and solutions from major cloud providers is driving the growth of edge computing, sovereign cloud, and cloud marketplaces.

- Capgemini and Orange announced a joint venture, Bleu, that will provide trusted cloud ("Cloud de Confiance") services for French organizations. Bleu's first services, including Microsoft Azure and Microsoft 365, will be operational in 2024.[97]
- Amazon announced plans to launch the AWS European Sovereign Cloud targeting highly regulated industries and the public sector in Europe. This independent cloud will be located within Europe, separate from AWS' other cloud operations, and it will allow only EU-based AWS employees to oversee operations.[98]
- Mambu, a SaaS cloud core banking platform, launched its solutions on AWS Marketplace and Google Cloud Marketplace in 2023, offering increased convenience and decreased time to market for new product launches for customers.[99, 100]
- Fujitsu conducted joint verification trials with Microsoft in Japan in mid-2022 to create a platform for collectively managing equipment from 5G base stations to edge applications using edge computing solutions. Following the success of its trials, Fujitsu planned to conduct further trials in the UK in an effort to commercialize private 5G and edge computing services.[101]
- SoftBank started nationwide deployment of multi-access edge computing (MEC) servers in Japan's Kantō region in May 2022, opening a 5G MEC site.[102]

IN A NUTSHELL

By combining the computational power of cloud and edge devices, financial services firms are looking to leverage the benefits of real-time insights, enhanced security, scalability, and cost savings.

- In July 2023, HSBC joined the quantum secure metro network of multinational British telecommunications company BT Group and Toshiba. Technology trials will test financial transactions, secure video communications, one-time-pad encryption, and the use of edge computing capabilities via an AWS Snowball Edge device.[103] The quantum secure network provides additional security to network infrastructure, independent of computational power. It offers a future-proof solution based on the l principles of quantum mechanics to guarantee the forward secrecy of encryption keys.
- In December 2021, Barclays partnered with HPE GreenLake, an edge-to-cloud platform that delivers cloud services that can run on-premises, at the edge, or in a co-location facility. The edge-to-cloud platform is an integral part of Barclays' hybrid multi-cloud strategy, hosting thousands of workloads and supporting the bank in providing a personalized banking experience for its customers.[104]
- In 2023, ING Bank, ABN Amro, Crédit Agricole CIB, The Bank of Nova Scotia, National Westminster Bank Plc, Banco Santander, and UniCredit Bank AG together committed EUR 725 million (USD 769 million) in financing for AtlasEdge, a pan-European edge data center provider.[105] Formed in 2021 when Liberty Global and Digital Bridge combined assets for a European-edge play, AtlasEdge operates more than 100 edge data centers in cities including Amsterdam, Barcelona, Berlin, Brussels, Copenhagen, Hamburg, London, Leeds, Madrid, Manchester, Milan, Paris, and Zurich.
- In 2021, J.P. Morgan spent more than USD 2 billion on data centers, citing the necessity for expansion into markets such as the UK. The trend indicates that data sovereignty - an edge computing driver - will be top of mind during regional infrastructure builds.[106]

Figure 7. Three frontiers of innovation for the cloud

Edge computing
by enabling real-time data processing and data sovereignty, will enhance the speed and dependability of bank services and bolster data security

Sovereign cloud
provides benefits such as increased security, control, and compliance with data regulations, thus also bolstering customer confidence

Cloud marketplaces
are enabling financial institutions to swiftly adopt innovative cloud-based solutions, through easily accessible services from different providers

Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

The edge and cloud computing fusion trend empowers banks to establish a technology infrastructure that is agile, secure, and efficient. Strategic deployment of edge computing solutions that enable real-time processing, combined with cloud scalability and advanced analytics capabilities, will help banks elevate service offerings, adapt to evolving customer demands, and maintain stringent security and compliance standards.

As the number of solutions on cloud marketplaces expands, it is increasingly convenient for banks to adopt cloud technologies. This not only streamlines procurement processes but also allows for quicker adoption of innovative technologies. Consequently, it boosts operational efficiency and enhances adaptability to a dynamic landscape.

We anticipate that more stringent regulations relating to data privacy and data sovereignty could also provide a push for sovereign cloud in 2024 and beyond. Regulatory mandates are particularly noteworthy considering the financial sector's vast trove of sensitive customer information, which makes it a target for cyber threats and security breaches. Edge data servers could also emerge as a crucial solution, enabling organizations to keep data within their boundaries and national borders.

TREND 8

Banks explore generative AI to elevate productivity

Generative AI is sweeping retail banking by enhancing customer service, refining decision-making, boosting efficiency, and enabling personalized products and services.

CONTEXT

A subset of machine learning (ML), generative AI is driven by vast datasets and advanced neural network architectures, making it capable of impressive and diverse outputs. Banks around the globe are considering generative AI's potential but are taking a cautious approach as they quantify its impact on data security and privacy. As the technology develops and banks identify use cases, they weigh benefits versus risks.

- Generative AI's impact on productivity could add trillions of dollars to the global economy, according to a Q2 2023 report from McKinsey. It could boost the banking sector's annual revenues by 2.8–4.7%, translating to an additional USD 200 to USD 340 billion.[107]
- Studies from Stanford and MIT indicate that generative AI improves output and boosts productivity, particularly for lower-skilled employees.[108, 109]

CATALYSTS

Generative AI technology is developing rapidly, and global demand for AI talent is surging. Applications require massive computing power, so data centers are scrambling to innovate to scale the technology.

- In a February to April 2023 global recruitment push, J.P. Morgan posted over 3,650 AI-related job openings. Reports indicate a fivefold rise in inquiries from banks seeking AI talent in the first quarter of 2023 compared with Q1 2022.[110]
- Generative AI technology is advancing with increased capabilities at a rapid pace. Just four months after the November 2022 release of ChatGPT – an AI chatbot that uses natural language processing to create humanlike conversational dialogue – a new large language model, GPT-4, was released with significantly improved capabilities.
- Similarly, in July 2023, four months after the release of the original Claude model, AI startup Anthropic released Claude 2, a new model of their AI assistant, which doubled the original model's parameters (860 million versus 430 million). Designers say the new version features larger text document uploads, longer context windows, faster outputs, and complex reasoning capabilities.[111]
- Japanese multinational investment company SoftBank and US-based NVIDIA, a leading AI hardware and software supplier, are collaborating on a platform for generative AI and 5G/6G applications that SoftBank plans to roll out at new, distributed AI data centers across Japan.[112]

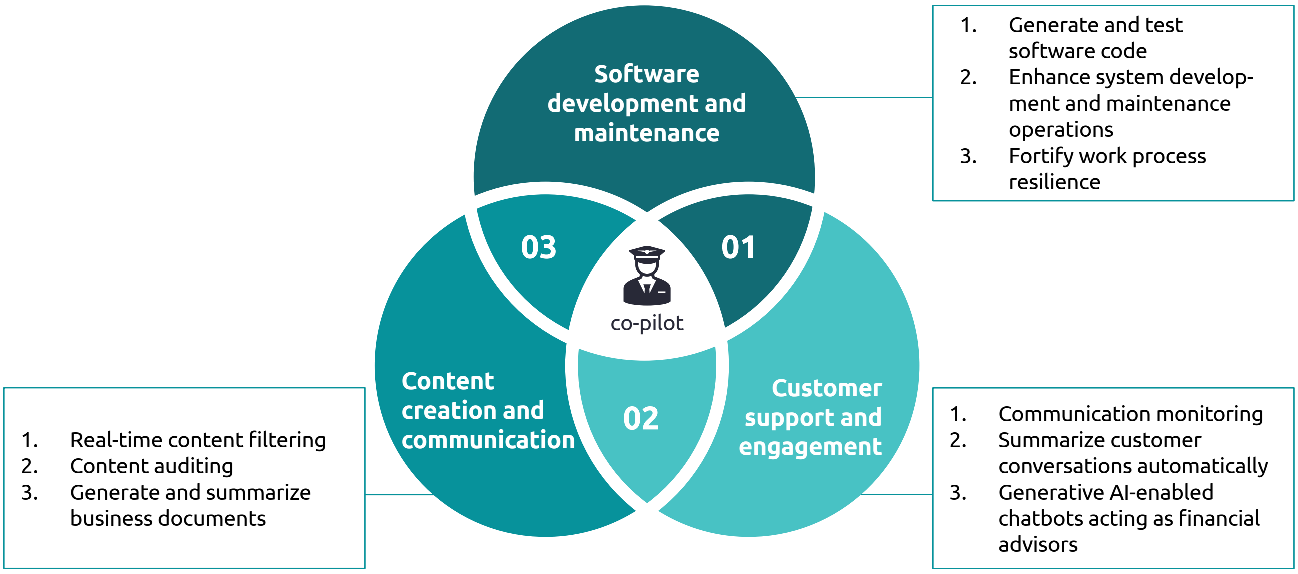
IN A NUTSHELL

Banks and financial institutions are embracing generative AI and conducting pilots to explore the potential impact on business operations. Multiple use cases are emerging, particularly around code development and customer service.

- Dutch bank ABN Amro uses generative AI to summarize customer conversations automatically. It also uses it to help answer queries.[113] Online-only Ally Bank piloted an AI-powered program to transcribe and summarize customer service calls. SouthState Bank implemented an enterprise version of ChatGPT in Florida, empowering employees to inquire about bank policies, compose emails, and translate meetings.[114]

- In November 2023, OCBC Bank, a leading Singapore-based bank, introduced a generative AI chatbot for its 30,000 employees globally to assist them with writing, research, and ideation. The deployment of the chatbot aims to further increase productivity and improve customer service.[115]
- Goldman Sachs is experimenting with generative AI tools internally to help developers automatically generate and test code.[116]
- In Dubai, Emirates NBD Bank is adopting generative AI and plans use cases across business lines.[117]
- Mizuho Financial Group is piloting generative AI to enhance system development and maintenance operations. Trials will evaluate AI's ability to autonomously identify errors and omissions in system design plans and auditing procedures. The objective is to fortify work process resilience by implementing generative AI in source code generation, system development, and maintenance tasks.[118] In Q3 2023, Hokuhoku Financial Group began use cases in Hokuriku Bank and Hokkaido Bank to respond to internal inquiries, generate and check various business documents, and create programs.[119]

Figure 8. Generative AI could be a productivity co-pilot across multiple business functions



Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

Banks and financial institutions globally are widely piloting generative AI applications. As more use cases and results emerge, banks will slowly but surely expand the scope of generative AI across the enterprise. Generative AI could permeate the entire value chain, from front-office customer interactions to middle- and back-office operations. Expect use cases including chatbots and virtual assistants, personalized communications, risk assessment, fraud detection, and streamlining of internal processes to boost efficiency and customer experience.

Generative AI adoption can be pricey because developing and operating AI systems is costly, particularly for advanced AI models that use deep learning techniques – such as large language models (LLMs). As future-focused banks consider generative AI in 2024 and the years ahead, they will strategically evaluate whether to partner with a provider, build their models in-house, or implement a hybrid plan. Hiring and upskilling will also be essential.

While AI may optimize performance, banks face ethical considerations, including algorithmic bias, security risks, privacy violations, and lack of transparency. Expect governance framework adjustments that consider new risk elements. Clear governance frameworks around policies, ethics, and usage will be crucial for deploying generative AI and LLMs.

TREND 9

Data is evolving from a proprietary asset to a shared, open resource

The rise of global open banking has catalyzed data into fuel that can empower banks to become further involved in customers' lifestyles and life cycles.

CONTEXT

The European Union led the way in open banking: regulatory bodies actively shaped frameworks and governing policies around open banking and laid the path for further adoption. Globally, open banking is growing, too – most often driven by regulators, as we see in Saudi Arabia, Australia and Brazil. Conversely, the United States encourages a free-market approach and is now introducing regulations to drive broader adoption.

A 2022 report from Allied Market Research projects that the global open banking market will reach nearly USD 124 billion by 2031, for a CAGR (2022 – 2031) of more than 22%.[120]

CATALYSTS

Increased consumer awareness and acceptance of how banks use their personal information – and a desire for convenient, retail-like customer service – are fueling open banking growth.

- The number of consumers and small to mid-size enterprises actively using open banking services in the UK crossed 7 million for the first time in January 2023.[121]
  - » In the United States, Visa's Open Banking Consumer Survey indicated that 87% of US consumers were using open banking to link their financial accounts to third parties.[122]
- The Consumer Financial Protection Bureau (CFPB) – an independent US government agency responsible for consumer protection in the financial sector – is working on a personal data rights rule to help consumers control their financial data. The regulation is slated to go into effect in 2024.[123] The CFPB framework mandates that banks provide qualified third parties with access to consumer financial data through the use of APIs. With many banks reliant upon legacy back-end systems, partnerships with FinTechs will likely increase. Meanwhile, FinTechs benefit from bank collaboration through first-hand access to data security best practices.[124]
- The EU introduced proposals to update the Payment Services Directive Two (PSD2). The new PSD3 and Payment Services Regulation (PSR) proposals were introduced to improve open banking competitiveness, protection against fraud, and other objectives.[125] They mark an important step towards open finance and are expected to be implemented between 2025 and 2027.
- The Saudi Arabian Monetary Agency (SAMA), the Saudi Central Bank, announced the Open Banking Framework which includes legislation, regulatory guidelines, and technical standards based on international best practices to enable banks and FinTechs to provide open banking services.[126]

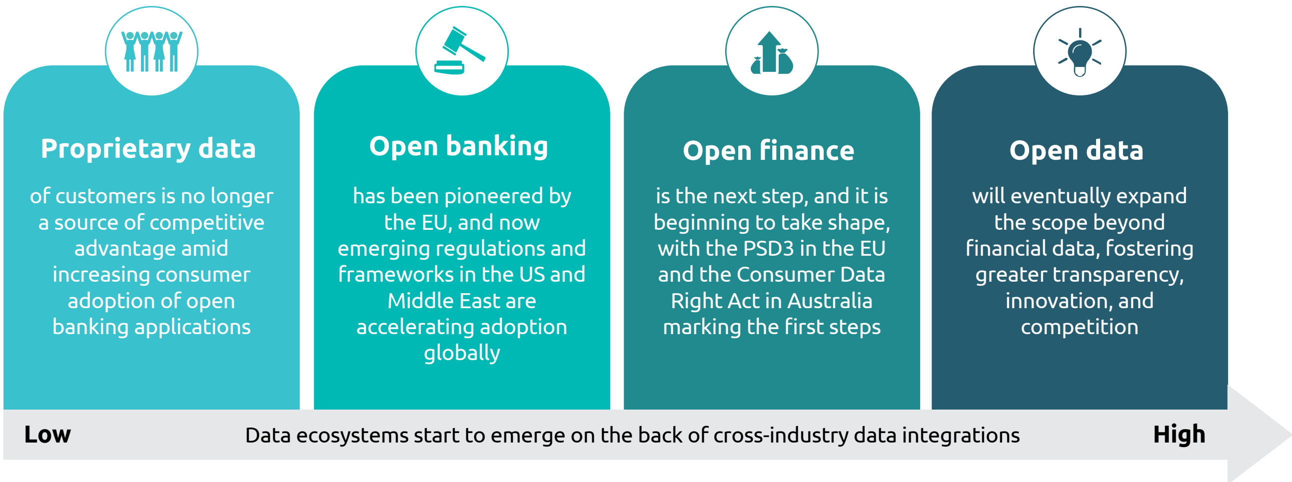
IN A NUTSHELL

The ascent of open banking is empowering customers to gain control over their personal information while driving product innovation. Results include improved customer experience and personalized offers.

- Mastercard expanded its European open banking capabilities in 2023 with a new account owner verification tool in partnership with Algoan, a Paris-based decisioning-as-a-service specialist.[127]

- In 2023, the Commonwealth Bank of Australia partnered with technology solution provider NextGen, an accredited data recipient under Australia's Consumer Data Right, to use government-regulated data sources to qualify mortgage applicants. NextGen's ApplyOnline feature auto-populates customer data and generates tailored bank statements for mortgage brokers to expedite approvals.[128]
- In 2023, ING partnered with Salt Edge, a FinTech open banking solutions provider, to offer a range of open banking use cases for small to mid-size businesses across industries.[129]
- In early 2023, Dublin-based multinational data analytics and consumer credit reporting company Experian partnered with London-based FinTech Zopa Bank (a provider of credit cards, savings, and loan products) to help customers take control of their credit scores by sharing data voluntarily. Now, Zopa includes Experian data within its credit card decision process.[130]
- In September 2023, BNY Mellon launched Bankify, in partnership with Swedish FinTech Trustly, to allow firms to receive customer payments from bank accounts.[131]

Figure 9. Banks are shifting from guarding proprietary data to embracing open banking



Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

Customers benefit from open banking because it gives them greater control over their data. It also allows them access to a broader range of services from different providers, leading to increased competition and better consumer deals. For banks, utilizing third-party data offers transformative opportunities with a high potential impact.

An emerging trend is the potential to forge innovative partnerships to develop distinct branded products. Increased competition will drive cost efficiencies and expand access to financial services. Also, as the regulatory landscape evolves, more bank/FinTech partnerships – driven by compliance and innovation – may emerge.

As the open data journey continues, expect more regulations in 2024 and beyond, such as the EU's Financial Data Access framework. The gradual shift to open data will help retail banks increasingly become lifestyle partners by embedding themselves in non-financial customer journeys beyond core financial products and services.

TREND 10

Decentralized finance continues to evolve; banks need to be ready for soon-to-come regulatory frameworks

2023 was a tumultuous year for DeFi, with compromised user data, money laundering claims, and hacked wallets that resulted in a regulatory push from authorities and demand for technological innovations.

CONTEXT

Amid muted consumer sentiment regarding decentralized finance (DeFi) during a prolonged crypto winter, banks and other financial institutions have continued experimenting with different use cases. Regulators are attempting to strengthen consumer protection and increase trust in DeFi. The EU's Markets in Crypto-Assets Regulation (MiCA), slated to go into effect in 2024, was to be a legitimizing milestone for decentralized finance in Europe. But, surprisingly, DeFi was excluded from the rules because decentralized applications (dApps) are not considered intermediaries. Now, experts warn that ignoring DeFi could undermine the effectiveness of the EU's regulatory framework.[132]

- Meanwhile, the US Senate proposed a bipartisan bill to impose bank-like regulations on DeFi.[133] The bill seeks to require those that control the protocol – or have invested more than USD 25 million in it – to vet and collect know-your-customer (KYC) information.
- Additionally, there is a need to monitor and report suspicious activities to regulators and maintain anti-money laundering programs.
- Hackers stole more than USD 3 billion in 2022, with the key source of vulnerability being smart contracts utilizing cross-bridge applications.[134]

CATALYSTS

The 2022 crypto winter following the collapse of companies such as FTX led to falling crypto prices and widespread skepticism that continued into 2023. Hacking further highlights the need for regulations in the sector. However, central banks globally have remained optimistic and continue exploring DeFi use cases with extended interest in CBDC.

- Capgemini's report "Building Central Bank Digital Currency" highlights that almost all central banks globally are exploring the CBDC opportunity. Representing 95% of global GDP, 114 countries are engaged in CBDC research and development, pilots, or actual digital currency launches.[135]
- Australia conducted its first foreign exchange transaction using eAUD in a pilot for the country's CBDC. The transaction was done on a dApp on an Ethereum layer 2 blockchain.[136]
- In September 2022, the Ethereum Merge transitioned Ethereum from proof-of-work to proof-of-stake, significantly reducing the energy consumption of DeFi on the Ethereum network. Data from The Cambridge Centre for Alternative Finance shows that Ethereum's energy use dropped by 99.99% after the Merge, resulting in a substantial decrease in DeFi energy consumption.[137]
- New regulations in the United States and Europe will offer more clarity with the promise of better security, a crackdown on illegal activities, and protocols that enhance cross-border transactions.

IN A NUTSHELL

The growth of DeFi and blockchain is leading to major banks developing frameworks, exploring multiple use cases through pilot programs, and tokenization of real-world assets.

- In Q2 2023, TransUnion, one of the three major credit agencies in the United States, began offering credit scores for DeFi lenders. TransUnion will provide traditional (off-chain) credit scores for individuals when they apply for loans on blockchain-based protocols without compromising applicants' privacy, the agency said.[138]

- Singapore-based DBS Bank became the first bank in Asia to complete an intraday repurchase transaction on a blockchain-based network. DBS completed the transaction on J.P. Morgan's intraday repurchase application Onyx Digital Assets, which enables instant settlements and transaction maturity within hours versus the more typical one to two working days.[139]
- In late 2022, J.P. Morgan completed its first live cross-border transaction on a public blockchain. Project Guardian of the Monetary Authority of Singapore facilitated the trade.[140] J.P. Morgan is also developing a blockchain-based digital deposit token for accelerating cross-border payments and settlement, and is awaiting approval from US regulators.[141]
- Citibank is also looking into tokenization. It is experimenting with a shared market utility using digital assets called Regulated Liability Network PoC with several banks and industry participants, which creates inter-operability between banks' tokenized fiat offerings, which it claims is the way forward.[142]

Figure 10. Six key drivers for DeFi growth

Lower Energy Consumption

The Ethereum Merge transitioned Ethereum from proof-of-work to proof-of-stake and has significantly reduced energy consumption

Interconnecting of lockchain Rails

Banks have continued to explore blockchain interoperability to integrate different blockchain networks

Bridging DeFi and TradFi

Convergence via partnerships, platforms, and innovations is making DeFi more institutional-grade, and TradFi more open and digital

Layer 2 Scaling

Layer 2 scaling solutions can provide faster and more cost-effective transactions

Modular Blockchains

Modular blockchains that allow for specialized sidechains provide flexibility and interoperability

Regulatory Frameworks

The US Senate proposed a bipartisan bill to impose bank-like regulations on DeFi

Source: Capgemini Research Institute for Financial Services analysis, 2023.

IMPACT

DeFi could see renewed consumer interest following the crypto fall of 2022, with regulations being proposed and implemented by the EU and US to protect consumers and increase their trust in the sector. Banks have continued foraying into the space with particular value seen in the tokenization of traditional assets, and multiple use cases are emerging around it, including deposit tokens. CBDCs also continue to be popular.

Blockchain interoperability and modular blockchains are also likely to gain in importance given their potential to increase efficiency and scalability. Pilots are starting to show results, particularly around cross-border transactions, with trades being executed successfully on a blockchain. With newer use cases, too, the success of initial pilots to validate the potential of the use case will be crucial for wider adoption in the industry.

The exact evolution of DeFi remains to be seen, but the potential for growth is immense with technological advancements as use cases become more widely publicized. Better security driven by regulatory requirements could lead to more stability in the sector and provide an impetus for renewed consumer enthusiasm, as well as broader adoption of the technology by banks globally.

CONCLUSION

What's in store for retail banks in 2024? Based on anticipated trends, firms will be required to balance business resilience and continuous innovation to navigate global macroeconomic complexity. Maintaining market position will be a challenge as new-age players, new technologies, and new regulations continue to transform the landscape.

After record outflows in early 2023 that marginally stabilized in the second half, banks have since been forced to compete through high-yield savings rates to hold on to and grow deposits. Even if interest rates go down in 2024, deposit costs are likely to remain high. Loan request volume is slow amid higher borrowing costs, and banks cautiously foresee a decline in credit quality and collateral value. Therefore, to maintain profitability, cost trimming, branch closures, streamlining of ATM networks, and lean operations will continue to be necessary.

Innovation will delineate competitive frontrunners from wait-and-see firms. While at-scale generative AI adoption could take time as banks conduct pilots, we anticipate the most high-impact use cases to move to the head of the implementation line. Open banking has fueled mainstream disruption as third parties now monetize firms' once-proprietary customer data, and banks must consistently add new value to retain top-of-mind relevance.

Sustainability and cloud are among the opportunities incumbents will likely tap in 2024. Banks will also ramp up efforts to cater to the affluent wealth band (those with investable assets of USD 250 thousand to USD 1 million): to be successful, firms will develop products and services tailored to their specific needs and craft premium experiences to secure long-term loyalty.

Finally, we recommend that banks fortify their digital operational resilience in the face of increased regulatory scrutiny, and take note of nascent regulations in the decentralized finance space as they continue to identify and test use cases.

The months ahead may open new doors for retail banks. While challenging economic conditions are not behind us, the initiatives of central banks have begun to show results. If inflation comes down to target levels in the latter half of 2024, then growth may pick up.

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