

WHITE PAPER

DIGITAL BANKING OVERVIEW IN THE PHILIPPINES

**How to Overcome Challenges
and Tap into Growth
Opportunities in Digital**

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EXECUTIVE SUMMARY

This document's objective is to highlight the main challenges of digital banking in the Philippines from the banks perspective and how banks should address these points. It also provides a digital banking market overview with an outlook on how this area can be more beneficial for banks and financial institutions.

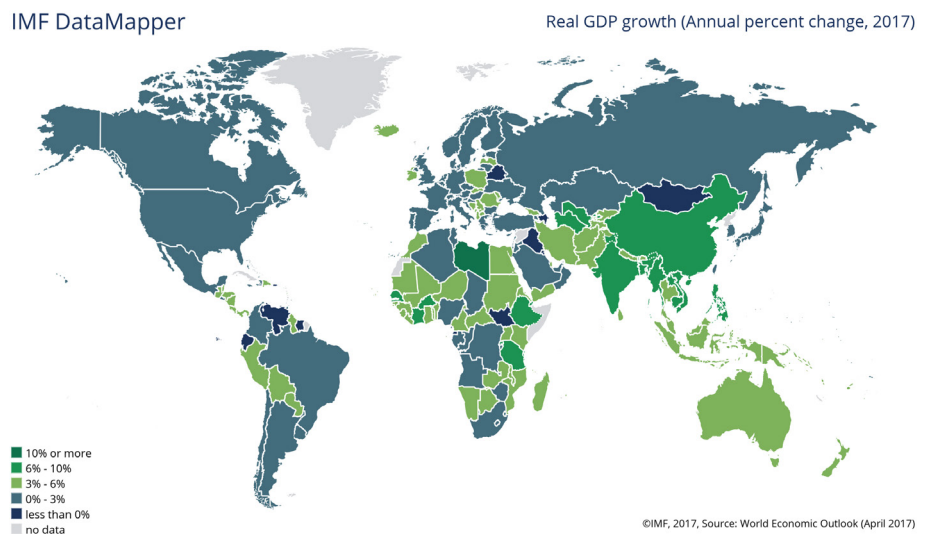
Digital - Just Not When Banking

The Philippines is one of the most dynamic economies in Asia, with GDP growth of 6.8% expected in 2017 and 6.9% in 2018. Banks in the country are well-established from a liquidity standpoint, and the central bank (BSP) fully adopted Basel III's Liquidity Coverage Ratio in 2016.¹

According to a study by consultancy Asian Banker Research, while the growth of retail banking income in the Philippines is expected to slow to about 12-13% (from about 17%) over the next few years, it will still be the second-fastest in the region after Vietnam.²

As a result of the anticipated slowdown, it is increasingly important for banks to look for new sources of income and control costs.

Figure 1: Real GDP growth (annual percentage change)



1. "World Economic Outlook (April 2017) – International Monetary Fund – imf.org/external/datamapper/datasets/WEO

Philippine Statistic Authority (PSA) – psa.gov.ph/

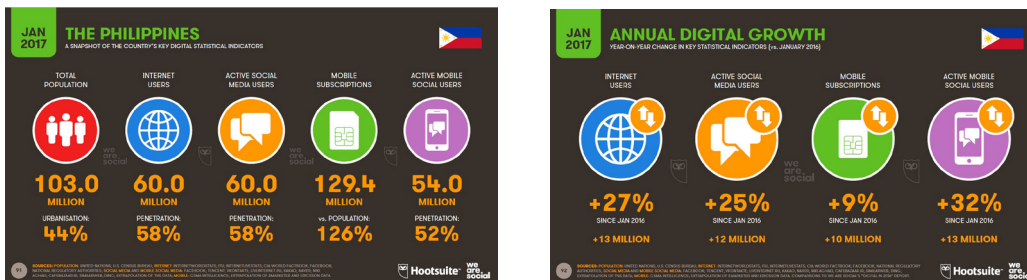
The World Bank – data.worldbank.org/country/philippines

2: The Asian Banker Research – theasianbanker.com/

Strong Economy and Growing Retail Banking

Although the Philippines took the global leader role in the “time spent on social media” category in the We Are Social and Hootsuite’s Digital in 2017 report, the current digital banking landscape in the country is not advancing in a similar fashion.

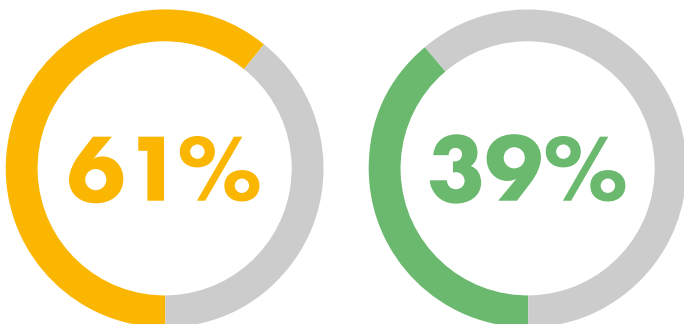
Figure 2: Key digital statistical indicators and year-on year change



In fact, the Philippines is the only country in the region where the majority of consumers prefer to pay bills over the counter, whereas in other countries consumers prefer to use banks’ websites, according to the Unisys APAC Banking Insights Survey, which surveyed people from the Philippines, Australia, Hong Kong, Malaysia, New Zealand, Singapore and Taiwan. Indeed, the survey also showed that 17% of Filipino respondents preferred going into a branch even when simply checking their account balance.

This reluctance of Filipinos to use digital banking is due to the lack of a compelling digital user experience that would encourage them to stop seeing branches as vital to transacting.

Population Owning Smartphones vs. Population Owning Computers



Meeting Customers' Expectations and Gaining Useful Insight

It is clearly true that customers' expectations towards digital banking evolve. In terms of digital, customers like to keep things simple and they expect a similar, personalized, omni-channel experience for handling their finances. Banks therefore have to deliver an engaging solution similar to that from Google, Facebook or Apple. These companies are successful because they focus on the user. They provide them with a superior user experience and once the users are hooked, valuable information can be gathered about them. This information is then carefully analyzed and can be used to sell them the most relevant products and services. The same can be achieved by banks, but they need to have a strategy, a journey that can be followed, polished and continuously improved, and it should begin with a customer-centric mindset.³

3. "Why Digital Transformation is a painful process for banks?" – Fabian Szijarto – slideshare.net/FbinSzijrt/why-digital-transformation-is-a-painful-process-for-banks

Improving Infrastructure to Reach New Markets

According to Akamai's Q1 2017 State of the Internet Connectivity Report, the Philippines is the lowest ranking among Asia Pacific countries for this metric, as well as some of the broadband adoption metrics, but at the same time it has seen a robust 20% quarterly boost in speed.

Significant improvements are expected in infrastructure as Philippine President Rodrigo Duterte has approved a plan to deploy a national broadband network at an estimated cost of between \$1.5 billion and \$4.0 billion to accelerate the deployment of fiber optics cable and wireless technologies to improve internet speed further.⁴

The network will be used to host a national portal and other online government services, as well as to connect remote areas of the country that are underserved by existing broadband providers to fast go-to-market strategies.

Figure 3: Average connection speed (IPv4) by APAC country/region⁵

Global Rank	Country / Region	Q1 2017 Avg. Mbps	QoQ Change	YoY Change
1	South Korea	28.6	9.3%	-1.7%
4	Hong Kong	21.9	-0.2%	10%
7	Singapore	20.3	0.8%	23%
8	Japan	20.2	3.1%	11%
16	Taiwan	16.9	7.9%	14%
21	Thailand	16	20%	49%
27	New Zealand	14.7	14%	40%
50	Australia	11.1	9.6%	26%
58	Vietnam	9.5	15%	89%
62	Malaysia	8.9	9.1%	40%
68	Sri Lanka	8.5	17%	58%
74	China	7.6	20%	78%
77	Indonesia	7.2	6.7%	59%
89	India	6.5	17%	87%
100	Phillippines	5.5	20%	57%

4. "Philippine Development Plan 2017-2022 – National Economic and Development Authority – iro.ph/article_doc/fc55bc53_PDP-2017-2022-Prepublication-2.pdf

5. "State of the Internet Q1 2017 report – Akamai – akamai.com/uk/en/about/our-thinking/state-of-the-internet-report/

The Essential IT Transformation

The majority of core banking systems in the Philippines were designed decades ago, when programming languages were entirely different, and that makes it extremely difficult for banks to keep up with modern, rapidly changing environments. Silo systems can also be a barrier to progress, especially when they prevent a bank having full access to its own data.

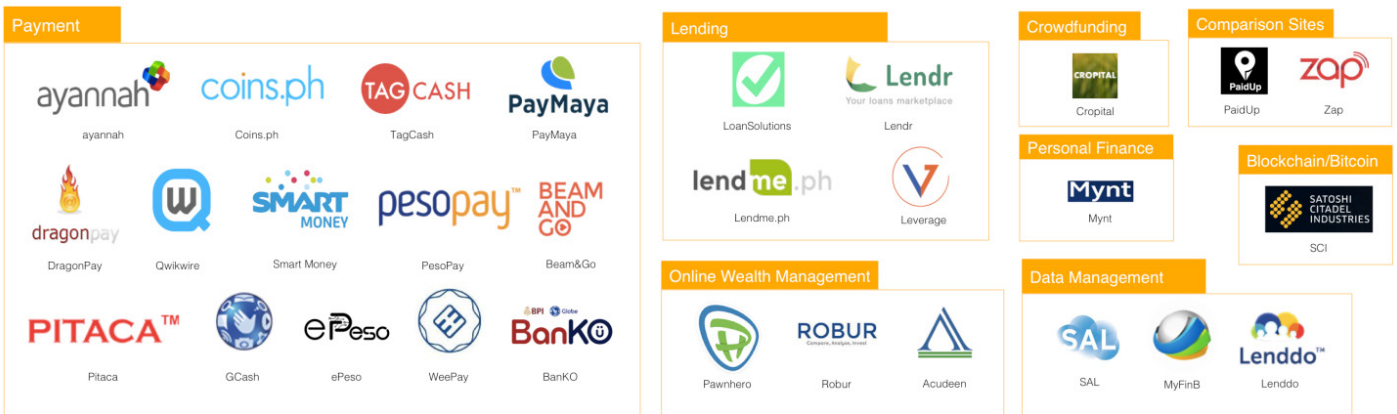
However, banks should invest in holistic IT transformation if they want to keep up with the competition and be able to adapt and respond quickly to changes, which is fundamental when it comes to fast go-to-market strategies.

Doing this certainly requires more than just a simple decision, since there are many inherent risks, but ultimately installing a 24/7, real-time solution based on open source technologies is vital. This does not mean that banks need to immediately plan for a rip and replace, but rather they should build a step-by-step, revolutionary IT strategy.

Vital Innovation and Open Infrastructure

Since a number of fintech players in the Philippines are already offering various disruptive solutions, continuous innovation and open infrastructure should also be part of a progressive strategy.

Figure 4: Top 24 fintech startups⁶



6. "Top 24 Fintech Startups – Forbes Philippines – fintechnews.sg/5978/philippines/top-24-fintech-startups-forbes-philippines/

Reaching the Unbanked with Digital



We have put in place policy and regulatory frameworks for the use and acceptability of financial technology. Since this is new to us, we have opted for sandbox approach so that we can test value propositions and allow them to evolve over time until we are completely convinced the idea is feasible and socially useful.”

Diwa Guinigundo

BSP Deputy Governor



only 14% of households have deposit accounts

Based on the latest data from Bangko Sentral ng Pilipinas (BSP), only 14% of households in the Philippines have deposit accounts. The majority of the remaining 86% unbanked are self-employed, working for a private household or in other informal occupations.⁷ The main reasons for not having an account are:

- Not having enough money to keep an account;
- Not having the need for a bank/cash account;
- The bank/institution location is too far away;
- They cannot manage an account;
- Service charges are too high and the minimum balance is too high.

These deterrents could be seen as opportunities that banks and financial institutions could leverage if they put an appropriate strategy in place.

Digital Client Onboarding

Attracting new customers and opening accounts for them using a mobile application is not only the most convenient way from the customers' perspective, but it is also effective for banks. Most of the banks, however, still struggle to take the first step.

Banks nowadays can use facial recognition and other biometrics for authentication and can leverage centralized data, which is usually provided by the central bank or by the government, to complete the required KYC processes.

Ultimately, regulations will determine what can and cannot be done digitally. KYC requirements are still rigid in some countries, but if the legal environment is not that favorable, banks can still focus on customer experience and make the onboarding and account opening process a lot easier than it is today.

Fortunately, BSP is continuously refining the rules and regulations to boost innovation to improve business actions in the financial sector.

7. "National Strategy for Financial Inclusion – Bangko Sentral Ng Pilipinas (BSP) – bsp.gov.ph/downloads/publications/2015/PhilippinesNSFIBooklet.pdf

Micro-Banking Offices (MBOs)

Banks can also reach out to the unbanked population by opening micro-banking offices (MBOs) in the Philippines. MBOs are low-cost banking infrastructures that can quickly and easily be introduced in municipalities where it is not considered feasible to set up a regular branch. Predominantly, MBOs focus on microfinancing; BSP is committed to further liberalizing them and allowing more functionalities, where relevant, in future.

While ordinary branches are concentrated in the National Capital Region, MBOs are more concentrated in underserved areas; hence, these municipalities can enjoy access to banking services through MBOs.

Latest data show the number of micro-deposit accounts had grown 217% to 2.9 million accounts in June 2016, from just 925,389 accounts in June 2012.

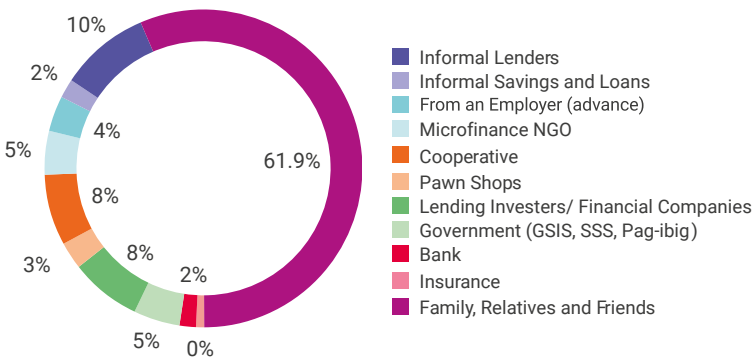
This is an excellent example of how financial institutions can successfully provide financial services outside urban areas.

Agency Banking

Agency banking is a model that helps improve financial outreach. Using this business concept commercial banks can contract third party retail networks as banking agents and these agents are then authorized to offer selected products and services on behalf of the bank. Since the agent is a commercial entity, it is equipped with the skills necessary to provide basic banking services according to standards set by the bank.

This will provide the opportunity to access financial products and services at the location nearest the customer, thus breaking down certain barriers to financial inclusion such as cost and accessibility.

Borrowers Preferred Fund Sources⁸



8. "Bangko Sentral NG Pilipnas (BSP), National Baseline Survey on Financial Inclusion: bsp.gov.ph/downloads/publications/2015/NBSFIFullReport.pdf

CONCLUSION

In summary, banks in the Philippines have all the necessary tools and a supportive regulatory environment to lead the country into a new era of digital banking. To start this journey and to exploit the opportunities, banks have to focus on and invest in their digital strategy, which should involve not only technology, but also process and organizational reengineering. This is a holistic approach and while there are risk factors, the truth is that the change is inevitable whether or not banks are ready.

ABOUT THE AUTHORS



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As solution consultant at Finastra, Fabian Szijarto is a subject-matter expert in digital channels. With over 12 years' experience in the FinTech industry, he specialises in digital banking transformation. Prior to his current role, he was senior pre-sales consultant at IND, a digital channels provider, driving workshops, proof-of-concepts and business analysis sessions. Previously, he held a number of roles at Raiffeisen Bank including consulting, product management and process engineering.



About Finastra

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