Tech Mahindra

DIGITAL TRANSFORMATION IN LENDING

WHITEPAPER

Connected World.
Connected Experiences.

A Point Of View

Decades of relevance and steady profits are not guaranteed for financial institutions (FI) anymore. Paper-based processes and inflexible underwriting processes mean that, traditional banks are slow to onboard new customers, slow to underwrite and unwilling to lend to consumers and entrepreneurs with limited credit history or track record. By contrast, fintechs/ new age lenders and alternate financial institutions have upped the ante by offering speed, convenience and seamless customer experience in the lending journey. Banks have also been very slow to digitize business banking, that has resulted in the eroding of market share and relevance, banks once commanded in small business lending. Inefficient and archaic systems notwithstanding, banks are equally burdened with uncertain regulatory environment, need for greater business agility and most important, customers that are more demanding and less loyal than ever.

Digital transformation of lending businesses in financial institutions should be driven as a prioritization of strategic principles for implementing digitalized improvements, service innovations and operational efficiencies. In the journey towards digital transformation, lending organizations should focus on digital imperatives that enable lenders to develop new operating models, products and services, while equally engaging with industry ecosystems to bring digital initiatives to scale.

Elucidated are essential initiatives that lending organizations should adopt to continuously cope with digital challenges from peers and disruptors alike.

Digitalization

The pandemic accelerated consumer demand for digital services and exposed the limitations of digitalization, scalability and agility of IT applications inherent in many financial institutions globally. Financial institutions have rejigged IT initiatives to cope with changes to operational procedures, new ways of collaboration with internal and external stakeholders, and increased focus on digital self-service, in the process of transitioning to what is interestingly coined as the 'new-normal'.

With digital self-service becoming the norm, financial institutions are enabling more services to be delivered through virtual assistants and voice / chat bots to provide virtual 24*7 support.

Most traditional organizations assume their journey towards digitalization is complete, as they replace legacy and manual paper-based process with digital functionality. However, that is only 'digitization' and not 'digitalization'.

Digitalization involves an outside-in approach as well as an inside-out approach to digitizing operations. The inside out approach encompasses modernizing legacy systems, integrating the full stack of credit applications including external systems, automating processes through deployment of bots, and achieving straight through processing for rapid response times.

The outside-in approach involves identifying the customer/ user journeys involved and developing responsive user interfaces, that deliver superior customer experiences while providing omni-channel capabilities for borrower credit journeys.

Omni-channel features in a digital lending solution enables channel switching, wherein a borrower can initiate a loan application from, say, a smart phone, however, complete it using his home computer, or by visiting a branch. While it could seem that the outside-in approach lays emphasis on the customer experience primarily, digitalization in the true sense is achieved only through digitizing the full stack of credit applications involving front, middle and back office processes.

According to 2020 Digital Banking Report research, only 66% of financial institutions with digital lending capabilities, enabled the entire loan application customer journey through disbursement to be completed digitally, with only 46% allowing end-to-end completion on a mobile device.

According to Gartner, 87% of senior business leaders say digitalization is a company priority, yet only 40% of organizations have brought digital initiatives to scale.

Digitalization

- Modernization of legacy
- API gateway for integrations
- Standardized credit process for cost savings
- Increased digital self-service with lower touch points
- Accelerated time-to-value with new products / services
- Customer service innovation

Collaboration Ecosystem

- Threat from alternate FI's
- Accelerated Digitalization
- Ecosystem of alliances for integrated propositions
- Profitable partnerships
- Expansion to new markets/ segments
- Trusted advisor for financial well-being

Customer Experience

- Behavior-driven UX-CX journeys
- Personalization for improved marketing ROI
- Omni-channel for consistent CX
- Seamless channel switching
- Accelerated digital adoption
- Lower cost of service
- Single view of customer

Analytics & Intelligence

- ML hyper-segmentation
- Differential pricing
- Augmented Underwriting
- Default / Churn Prediction
- Increase Customer Lifetime Value
- Next best product recommendation
- Loyalty /Retention mgmt.

Automation

- Cognitive Robotic Automation
- Multi-channel digital self-service
- RPA in loan document mgmt.
- Improved productivity, SLAs, quality
- Virtual assistants & Chat bots
- Parallel processing for reduced TAT & AHT
- Handling transactional spikes

Open Banking and Ecosystems

Fintechs and challenger banks have managed to erode the market share of traditional banks, especially in unsecured lending by providing speed, convenience and excellent customer service to consumers. Such alternate financial firms deploy digital-native lending solutions, enabling rapid development, launch of new products and fine-tuning of existing offerings as per changing needs and expectations of the consumer. Alternate financial firms are discovering unidentified consumer segments through hyper-segmentation to provide unique offerings. Examples include sports financing, healthcare equipment or treatment costs financing and the like. Additionally, they also serve thin-file customers that are new to credit and underserved segments that are usually turned down credit by banks, due to lack of formal credit sources for underwriting their credit requests.

Banks cannot turn a blind eye to this anymore. They have to either digitize their credit processes and infrastructure to compete with alternate FI's, or alternately partner with them to offer new products and services to retain their existing customer base and attract new customers. For both options, banks have to accelerate their digital transformation journey to open up their infrastructure and data through secure application programming interfaces (APIs), for consumption by third party systems and providers.

This will enable banks to forge profitable partnerships and open new pathways for innovation in customer service and expansion in business models. This is also an opportunity for banks to monetize data, improving top line while staying competitive and relevant in today's financial ecosystem.

Consumers are increasingly expecting integrated propositions from their trusted financial institutions for addressing their core needs. A home buying solution could encompass not just a mortgage loan but also include home insurance coverage, loan for home furnishings and the like. To provide such integrated propositions, banks have to transform into a trusted advisor with an ecosystem of alliances that deliver integrated propositions around core customers' needs.

As per industry estimates, digitalization initiatives in the form of service integration and reduction in bottleneck could result in up to 20% higher TAT and 15% faster time to market.

Regulations such as Open Banking in the UK and the Payments Services Directive II (PSD II) in Europe, combined with the EU's General Data Protection Regulation require banks to make data accessible to third parties, while offering pricing transparency and greater value to the consumers. Consumers are normally willing to share their data for reciprocal benefits.

Customer Experience Management

Central to the digital loan journey is the borrower's experience in the lending process, with an expectation of cutting-edge UX, personalized service and speed of processing. Developing behavior-driven user experience mapping for UX-CX, and simplified and intuitive customer journeys from start to finish of a credit lifecycle, is key to achieving exceptional customer experience management.

As customers switch between channels for various interactions during a credit journey, it is imperative to maintain a consistent brand and channel experience across channels.

Offering innovative, intuitive user interface for your digital customers is just one piece of the customer experience puzzle. The larger and important piece is 'personalization' in customer experience. Personalization improves customer loyalty and increases brand advocacy through valuable and memorable interactions that a customer has with an organization. This is by far the best form of advertising any organization can aim for: right message, right place, right time – every time!

Only 14% of global financial services firms believe that they have the right technology infrastructure and applications in place to deliver great and differentiating CX. However, more than 80% believe that they will be in this desirable position in 2024

Personalization requires organizations to gain in-depth understanding of their customers, by consolidating customer data from multiple systems, to enable a single view of the customer. Harnessing customer data gathered across several touch points, interactions, channels - online and beyond, and extracting meaningful insights on customer behavior and preferences, helps in providing personalization.

Personalization should not be restricted to only products and services, rather should be extended to customer messaging and communication as well. Lenders should strive to go the extra mile to genuinely offer personalized advice to their customers, for their customers' financial well-being.

Customer Experience Management involving redesigning and implementing product and service experiences can lead to a 20%- 30% uplift in customer satisfaction.

Analytics and Intelligence

Banks possess the most valuable assets necessary for winning in the digital economy – Data. Data driven analytics in the form of MIS and BI are widely used by enterprises for analysis of business information and improved decision making. Advanced analytics developed using machine learning (ML) technologies has gained prominence in lending institutions, involving various stages of the lending lifecycle such as customer acquisition, credit underwriting, loan servicing, collections and recovery.

For the customer acquisition process, ML based hyper-segmentation modelling is used for prospect segmentation and segment prioritization. Right offers are identified for targeted segments to increase conversion rate, thereby improving ROI on marketing campaigns. Analytics on customer data helps in applying differential pricing for credit worthy and loyal customers, thereby achieving personalization.

AI /ML is extensively used for augmented underwriting, that leverages alternate data to score new-to-credit or thin-file customers. The credit decision framework takes as inputs various data sources and generates a credit score, enabling automated decisioning or providing inputs to relationship managers for real-time credit approval decisions.

Research indicates that it is 6 to 7 times costlier to acquire a new customer than to retain existing customers. Advanced analytics for customer retention uses prediction models based on customer behavior, risk and usage patterns to make recommendations on "NEXT BEST PRODUCT" offers to consumers.

Preventive Risk Management for booked portfolios such as predictive delinquency and early intervention analytics lends itself to smarter collection and recovery strategies to reduce default rates.

To stay competitive, organizations need to leverage advanced analytical capabilities to anticipate new trends and develop strategies and actions to respond to changing market conditions.

As per industry estimates, analytical insights derived from a single view of customer, can lead to increased engagement up to 24% reduction in churn rate, and 20% greater customer engagement.

Automation

From conversational AI in the form of chatbots that are trained to deliver context-based service to its customers, to Cognitive Robotic Process Automation (RPA) enabling banks to intelligently automate manual credit processes for increased efficiency and reduced costs, Artificial Intelligence (AI) is all pervasive in financial institutions.

The typical use cases for automation in credit processes are related to loan document management, though RPA is prevalent in various front, middle and back office processes in the credit lifecycle.

Front office automation in the form of multi-channel digital customer service, leveraging virtual assistants and conversational AI, provide personalized digital customer service, resulting in every user getting a different experience based on data gathered around him/her.

From using RPA and OCR/ICR technologies for loan document capture to Cognitive RPA for data extraction, indexing and classification, RPA and AI technologies play a vital role in improving productivity, SLA's and quality adherence in the loan document life cycle.

Intelligent bank office for service request automation, incident automation and automated transactions leverage RPA and AI technologies for seamless collaboration and parallel processing to reduce average handling time (AHT) of service requests considerably.

Intelligent process automation can yield significant tangible benefits in the range of up to 20% by way of reduction in AHT, TAT, reduction in FTE and increased accuracy.

Summary

Financial Institutions should find the right balance of digitalization, as per their business priorities and organization culture. The spectrum spans from 'digital optimization', aimed at achieving operational efficiencies to 'digital transformation' or 'digitalization', which serves as the bedrock for a competitively robust, digital business model. FI's will need to evaluate the business vision of their organization, IT investment, innovation strategies, capabilities and expertise of their teams and accordingly prioritize execution and delivery of their digital strategy.

Customer attitudes, behaviors and aspirations will be the driving force of change in financial institutions in the future. Banks will need to transition to a realm of adaptive banking, from being product-centric to customer-centric, delivering finance that is integrated well into customers' lifestyle and expectations, to derive maximum value to stakeholders.

'Data is King' as long as financial institutions know how to effectively operationalize it. Most FI's have invested resources into building data management solutions to efficiently harness data, however very few have leveraged the data to develop a cohesive business strategy that is customer-centric. Analytical -insights driven strategies are a great differentiator for FI's in the hyper-competitive credit business.

References

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Gartner study on Digital Optimization and Transformation in Banking

From Convergent Experiences, an intelligent symphony of technology platforms & solutions for Human Experience to TechMNXT, powered by disruptive technologies, non-linear growth with platforms, and collaborative disruption with new age partners, Tech Mahindra's holistic approach to be future forward, strives to be a 'Value Partner' to financial institutions in their journey towards lending transformation.

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Jayashree Thandu is a Principal Consultant at Tech Mahindra and leads the Lending Competency practice. In Tech Mahindra, Jayashree brings her lending knowledge to bear, to design compelling solutions for lending organizations globally, leveraging Tech Mahindra's state-of-the-art lending projects and its partnerships with innovative software product vendors in the lending space. Jayashree has over two decades of experience and has worked in Solution Sales, Consulting & Strategy and Operations in IT Product and Services organizations. Jayashree has been associated with Banking for most part of her career, notably in Lending solutions and products for the past 10 years.

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