An occasion for online banking to capture laggards

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I recently walked to the grocery store in my little town in Piedmont, in the north west of Italy. Lockdown conditions were fully in place and, on the way, I walked by a bank. A long queue was standing there waiting to withdraw money from a cash machine (use of cash in Italy…). As I walked past, I heard an attendant from the bank asked a nice old lady if she could assist. The lady answered: "I'd like to donate to the Red Cross for the covid emergency and the television mentioned I could do this via a payment slip."

This true story illustrates one of the ways in which Italian banks lag. The country has 485 banks, over 24,000 branches, and 282,000 employees. In other words, the Italian banking system still relies on physical presence and proximity to serve customers. This is also due to demography and concentration of the wealth in older part of population but, as a result, Italy is one of the laggards in the use of online banking in Europe.

When will Italy evolve to a digital approach, for the low-value added services at least? The answer would have been different until a few weeks ago. Of course, there was a structural trend towards online banking but it was slow. The aging population coupled with low GDP growth suggested that a large part of the Italian wealth was going to change hands gradually, and new generations will prefer other channels to branches over time.

Now, the covid-19 emergency has accelerated the trend. During the lockdown, customers have been encouraged to use online facilities before going to a branch – normally branches open a couple of days per week, and receive customers by appointment only. The first anecdotal evidence of a faster-moving trend is the boom of requests to call centres to teach first-time users over 65 years old how to setup usernames and passwords they can easily remember.

Inexperienced customers are to not the only ones to blame though because, frequently, digital interfaces are not as user-friendly as they should be. This is changing quickly. Over the last few weeks, banks made some efforts to improve their platforms; however, considering massive investments in technology they were planning for the next few years, they might need to spend more to be up to speed later in the year.

If lockdowns are prolonged or reinstated, new fin-tech or existing diversified financial companies whose model is already fully digital can benefit from the "occasion" to show clients how easy is to perform banking transactions via their apps. This might allow them to steal market share to traditional players – even in Italy.

Still, among established players, there could be also be two relative winners: 1) asset gatherers and 2) Poste Italiane. Let's see why.

Asset gatherers have already been winners in Italy. Since the financial crisis in 2008, their market share has increased from 6 per cent to 14 per cent looking at the total Italian families' wealth, or from 13 per cent to 25 per cent looking at managed assets only. The asset gatherer model does not envisage any form of physical presence, but counts on a network of financial advisors, working as tied agents for each firm, and on advanced technology platforms. Some asset gatherers acquire new clients via financial advisors only, others also directly via their online channels.

In both cases, the model works perfectly these days. In fact, financial advisors do meet clients face-to-face normally, but for some time, they have been able to sign contracts and more broadly advise clients remotely, thanks to fancy apps, which are bulletproof from a compliance perspective. This is the perfect mix of human interaction and digital tools.

The covid-19 crisis might lead to three incremental opportunities for asset gatherers. First, the sell-off in all asset classes has increased the importance of advisory. Financial advisors know how to reassure /retain/expand a client base under emotional pressure, perhaps better than the average branch employee in a traditional bank. They are entrepreneurs; their salary depends on their success (and from the company standpoint, their cost is fully variable). Second, the higher capital ratios and the lack of asset quality concerns of asset gatherers compared with banks could lead to a "fly to quality" in term of deposits, for those who own a banking licence. In order to make money out of those deposits the asset gatherers need to convert them into assets under management, but, again, they are used to deliver on this.

The third opportunity is that the technology platforms of asset gatherers are new, simple, structured to be flexible, and user friendly. Some among them might be stronger than others in this respect, but they are all stronger than banks at first glance. The scalability of their models is generally huge. It would not be surprising to see more advertising and ad-hoc commercial campaigns to remind possible new customers about their pure online banking services (by the way, these are typically quite cheap given wealth management is the profitable area).

Poste Italiane might look like a typo in the article. A state-owned company with 12,800 postal offices and 126,000 employees, it is present in every little town in Italy. Weirdly, it does not come across as the most digital example that can be mentioned. However, Poste has developed strong digital internal knowhow and this has allowed it to convert some of its key activities, including financial activities, from physical to digital in a few weeks.

Before the pandemic, Poste already had 1.4m visits in their postal office, but also 2m daily on-line users. The latter appears to have increased dramatically in March and April. The customer experience in the online Poste app and website is good: simple, direct, user-friendly and integrated. Since March, new payment products have been available online, and Poste can distribute traditional products as postal savings with a physical history of over 150 years in the digital space too. In wealth management, Poste has just launched a new partnership with the fin-tech Moneyfarm which will help to capture new clients where the business proposition is based on cheap but high quality services thanks to robot advisory and exchange-traded funds.

So what about banks after Covid-19? Benoît Cœuré, Head of the Bank for International Settlements Innovation Hub said "Will customers find their way back to banking branches when lockdowns are lifted and economies restart? Will this accelerate the shift towards virtual banking? Issues such as tokenisation, open banking, and using technology to support regulatory and supervisory compliance ("regtech" and "suptech") are high on our agenda."

The answers to these questions will depend on the depth of the current crisis. Banks might not be able to rapidly invest in new technology to the extent they should, under severe and prolonged pressure. Meanwhile, in a more benign scenario, potentially also thanks to mergers and acquisitions, and the rationalisation of other expenses (more working from home, less branches and real estate costs, less travels) they could face the transformation more pro-actively.

Regardless, the opportunities for other financial players with more flexible models are huge: in the retail space in particular, to survive, banks need to move towards their model and this tells a lot. In a world of growing importance of ESG dynamics, all pointing towards a wider use of digital channels, we wonder why banks should move backwards. Legacies from the past might still be a problem and pose important social dilemmas to solve, but the current pandemic crisis is the occasion to work to a constructive solution.