



Realizing the digital promise

Top nine challenges to digital transformation in financial services - A summary

A paper from the Institute of International Finance and Deloitte

Disruptive forces continue to shape the future of financial services ranging from open data and changing customer expectations to disintermediation of the value chain and an evolving competitive landscape. In response, many financial institutions are embracing digital innovation to help them make the most of these shifting market dynamics, using responsible, data-driven insights to evolve their value propositions and realize the benefits of digital transformation. However, there isn't one uniform approach to digital transformation, with its scope, leadership, scale, and timing varying widely around the globe.

The Institute of International Finance and Deloitte have joined together to explore financial institutions' approaches to digital transformation around the globe, the common challenges they encounter, and the learnings these organizations share. The focus areas of our three-part series, to be released over the coming months, are: (i) challenges and barriers to digital transformation; (ii) enablers to capture more value; and (iii) the impact of risk on internal and external stakeholders.

This overview document previews the top nine external and internal challenges to digital transformation that we identify in the first paper. We have found these major challenges to consistently resonate across the globe, but with some occasional local variances that might intensify the impact of an individual factor, depending on different regional starting points and/or other local conditions.

The first paper draws on targeted research, workshops, and interviews with more than 60 global financial institution executives, regulators, and policymakers.

External challenges

#1: Investor expectations for financial institutions constraining digital transformation efforts

Investors of mature financial institutions tend to have a lower risk tolerance compared to investors of start-ups and FinTechs. As such, mature financial institutions often have a different level of expectation when it comes to making investment decisions on transformation initiatives. This can run counter to the key attributes of risk, experimentation, and learning through iteration that can be critical to business model transformation and innovation—and often makes investor expectations difficult to manage along the transformation journey. Standards and guidance around the world are eliminating many of the gaps in the system which can be exploited.



#2: Inconsistent data regimes restricting financial institutions' ability and appetite to generate value

Financial institutions have access to a great amount of customer and transaction data. However, inconsistent approaches to balancing consumer protection and innovation as well as asymmetrical requirements on data sharing frameworks in an open banking regime can create constraints on the use of data, putting financial institutions at a disadvantage. In addition, changing social norms around data security, customer privacy, and ethical use of data are making it increasingly challenging for financial institutions to leverage data to develop meaningful analysis for the purpose of transformation.



#3: Lack of enterprise readiness and capability by FinTechs limiting the ability for partnerships with mature financial institutions

Most financial institutions acknowledge that building an ecosystem of alliances and partners is important to success in today's current environment of disruption. However, FinTechs are often not subject to the same level or degree of regulatory and risk management. They also may lack the experience and expertise in integrating at an enterprise level of legacy technology and the complexity of operating processes. This means financial institutions should find the right FinTech partners who meet enterprise requirements and share the same values and vision.



#4: Prescriptive and/or outdated regulations constraining large-scale digital transformation initiatives

There is a degree of consensus among most initiative participants that financial institutions face different regulation and supervision compared to start-ups and FinTechs. This may prevent many from experimenting with more innovative transformational initiatives. Financial institution leaders surveyed would prefer for regulations to be principle-based and technology-neutral and to be complemented by supervision and guidelines so that regulation and supervision can be more agile.



Internal challenges

#1: Evolving talent models forcing many financial institutions to rethink the workforce of the future and the environment needed to retain talent

The composition of talent continues to change as most financial institutions become increasingly digitally enabled, with leaders challenged more and more by talent retention than recruitment. There is a growing demand for employees with data, design, and technology skills combined with business savvy and a willingness to be hands-on. Many FinTechs and technology firms are competing for this same rounded individual. Financial institutions should create and foster an environment with purpose and continued challenging work in order to retain this highly sought-after workforce.



#2: Lack of enterprise agility, understanding, and coordination for activating innovation partnerships

It is generally observed that forming innovation partnerships can help the financial institution accelerate digital transformation through impact on culture, mindset, and technology. However, onboarding FinTech partners often comes with a long lead time. This is partially due to a financial institution's risk, compliance and legal functions building their understanding of the FinTech ecosystem, causing delays to internal approval processes. The organization's internal functions may misinterpret certain regulations as prohibiting innovation partnerships, particularly in cases where there is an absence of supervisory guidance.



#3: Traditional risk-conscious culture clashing with a higher risk appetite for pursuing innovation

Digital transformation can be as much a human capital and mindset transformation as it is a technology transformation. Financial institutions often experience resistance to change because of their risk-conscious culture. It is important to align with key stakeholders on the "why" behind transformation and build a culture that allows risk taking and experimentation.



#4: Management ambition to meet short-term business targets misaligning with organizational needs for longer term transformation

Many transformation initiatives are led by executives that are responsible for the current and immediate business model, resulting in potential conflicts that impact the measure of their (personal) success. This can be particularly true in banking, where business decisions often have a more immediate impact on current year business outcomes than in insurance. A challenge is that manager performance scorecards are often based on short-term deliverables, whereas true transformation may take a longer timeframe to complete. Financial institutions should rethink performance metrics so that they incentivize the right transformation behavior.



#5: High regulatory-driven change burden leaving insufficient budget, resources, and management attention for digital transformation initiatives

Financial institutions struggle with achieving profitable growth amid a challenging macro environment and the high cost of meeting regulatory compliance requirements. Short-term profitability targets can impact organizations' R&D investment in longer term, strategic initiatives, resulting in little to no budget for large-scale digital transformation.



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