Digital transformation is changing risk management in banks

For some time now, banks have been using digital technologies to help transform various areas of their business; in fact, digital has become deeply embedded in banking strategy.


Richard Firth, CEO of MIP Holdings

Digitisation is compelling for financial services businesses across the board, as it promises significant advantages it brings in terms of customer experience, new revenue streams, and lowered expenses.

“Just look how many bank branches are being closed throughout the country. My calculations show that between the big four banks, over 700 branches have been closed in the last decade, bringing the era of self-service and less human interaction to the fore,” says Richard Firth, CEO of MIP Holdings.

He adds that there’s no doubt that ‘digital’ is changing the face of banking, and bringing with it a slew of new trends and risks.

> *“The face of risk management in banking has totally changed over the last decade, mostly thanks to regulations that were created in the wake of the global financial crisis and the massive fines levied in the aftermath. However, I believe risk management is set to see even more pervasive change in the next ten years.”*

Firth says, as regulation continues to broaden and deepen, we are likely to see increasingly stringent regulations, even for financial institutions operating in emerging economies. Over and above stricter regulations, banks are now expected to have means in place to help crack down on illegal and unethical financial transactions such as money laundering, fraud, and the financing of terrorist activities.

The strict implementation of ‘know your customer’ (KYC) is a prime example of how banks are expected to carry out due diligence to fight these scourges.

The changing face of the customer

The way banks treat their customers is also under the microscope, he says.

“Terms and conditions of contracts, marketing, branding, and sales practices are becoming increasingly regulated to protect the customer. In fact, under the terms of the Consumer Protection Act (CPA) banks are prohibited from behaviours that negatively affect consumers, including barriers to switching banks, inappropriate or incomprehensible advice, and non-transparent or unnecessarily complex product features and pricing structures.”

Another major change that is affecting banks across the board, he says, is the change in customer expectations.

“Advances in technology are facilitating a new customer experience. Customers today have access to more information and more products and services than ever before, and expect instant satisfaction, at any time, from any device. If they don’t receive what they want, when they want it, they will simply move to a competitor.”

Transformation in the banking environment

This is compounded by the rise in new fintech startups who do not want to be banks, in and of themselves, but want to rather hijack the direct customer relationship, and in that way, take a slice of the most profitable part of the value chain: origination and sales.

“Straightforward and seamless applications that fintechs provide are weakening the grip that banks have on their customers. Banks have to seriously look at how they deliver services and customer experience if they want to remain in business. Consumers want instant, customised services that are tailored to them, and again, this will probably see increased regulations to manage the associated risks,” Firth says.

“Remember, any changing environment brings new risks. Banks’ risk functions will now need to detect and manage a slew of new risks. Model risk, cybersecurity risk, and contagion risk are examples that have emerged. To prepare themselves, the risk-management function will have to build a perspective for executives on risks that might arise in the future, the bank’s appetite for assuming them, as well as means to detect and mitigate these risks. It will also need to be flexible enough to adapt to any new and unforeseen risks.”

According to Firth, all these elements mean that a high-performing risk function will be essential in the years to come. “It will have to be a key element of all banks’ strategic planning, and it will need the ability to manage multiple risk types while complying with current regulation as well as preparing for future regulation. Risk function will change significantly over the next decade, and banks need to get on board now if they hope to equip themselves with the capabilities needed to cope with new demands. I believe that these risk functions are going to complicate the rise of pure digital banks.”