

Is BaaS for Everyone? Why are Traditional Banks Hesitant to Adopt BaaS?



The 'Future of Banking in South Africa', an Executive Roundtable hosted by SunTec Business Solutions was held in Johannesburg, South Africa on March 9, 2023. The event brought together leaders from prominent banks in South Africa and from SunTec for a candid discussion complying to the Chatham House Rule around the various impacts on the banking industry and its outlook in the region. The delegates deliberated and shared opinions on the following key focus areas for the South African banking industry:

1. Banking-as-a-Service (BaaS)
2. Environmental, Social & Governance (ESG)
3. Dynamic Segmentation

This report summarizes the key points discussed during the session on Banking-as-a-Service (BaaS), moderated by Amit Dua – President, SunTec. Interesting perspectives emerged from the discussion. This report will help readers gather an understanding into the relevance of BaaS and how it plays out for different banks.

The context of the discussion was set with an example from the UK banking industry. New banking licenses had not been granted in the UK for over 60 years, but 47 new licenses were granted to organizations (mostly challenger banks and neo banks) to operate as banks in the last 10 to 11 years. This opened the conversation to the challenges traditional banks face with respect to new-age banks and their inherent technical advantage.

Understanding whether “BaaS is like SaaS?” helps banks gather insight into the value proposition of BaaS for banks. BaaS has also gained significance across many economies with new banking regulations that facilitate ‘Open Banking’.

BaaS is Not Just about Technology to Enable Banking

Technology is an integral component to enabling BaaS, but it is much more than just technology. It is also about enriching the customer experience and providing them a frictionless experience to banking. BaaS is not just about enabling technology but is an actual service that the bank offers in partnership with other service providers.

Buy Now, Pay Later

An individual shopping for furniture at an IKEA outlet could be supported with a 'Buy Now, Pay Later' service offered by a bank. The IKEA outlet functions as the touchpoint for the customer and the bank to interact while helping the customer avail of a service or product offered by the bank. The onus is on the service partner, in this case, IKEA to complete all KYC processes, and offer the customer a loan through the bank to facilitate the purchase of furniture.

Moving Away from the Core Identity and Branding of the Bank

A BaaS environment entails banks moving away from the limelight, as the attention would be more on the service partner enabling the transaction on behalf of the bank. The panel of speakers suggested that banks must be willing to let the retailer or distributor take the lead and be prominent while enabling the service, rather than holding on to their own branding or being at the forefront.

A New Business Model that is Not Relevant for All Banks

BaaS as a business model may not be relevant to all banks. Traditional banks with their regular customers and standard products and services are happy with existing business models and are not necessarily looking to experiment with BaaS. On the other hand, banks that are looking to venture into newer markets/territories and seeking new customers are more likely to invest in BaaS.

Differentiation Based on Service and Customer Experience

Banks that are already offering stellar services to their customers and providing them with a delightful customer experience will not try out new offerings with BaaS and are highly unlikely to make any changes to a system that works fine for them. They would rather invest money and effort into refining their existing customer experience, enriching it, and up-selling products and services to their existing customers.

Compliance and Regulations Will Play a Big Role in BaaS

Further, banking regulations vary from country to country and greater clarity is needed on partnerships, pricing, and risk factors in BaaS. In this [article](#) from December 2022, the author Yizhu Wang stresses on the huge role of compliance in the BaaS sector. Banking regulators are focusing their attention on third-party risks faced by banks in their partnerships with private fintechs and other organizations. Here is a relevant quote from the article – “Despite posing higher regulatory risks, the BaaS business model has yielded favorable financial results for the existing bank players compared to the industry average.”

This augurs well for banks looking to venture into BaaS, but it remains to be seen if success in North America can be replicated by regional banks in South Africa.

Partnerships – The Crucial Piece in the BaaS Puzzle

Deutsche Bank partnered with WeChat in China to offer banking services within the WeChat App itself. This offers a direct interaction opportunity for the bank with about 850 million unique users on the app every single day. Similarly, the leading Spanish bank, BBVA offered cab drivers access to a new credit card from within the UBER app. The primary focus is on providing customers with a frictionless banking experience facilitated by the retailer or service partner.



Traditional Banks Using BaaS and Digital Banking to Counter the Challenge of Neo Banks

The last few years have seen an increase in banking regulators granting banking licenses to non-traditional banking entities. Fintech startups backed with investor-money operate as mobile-first / digital banks. Termed as neo banks, the entire process of opening an account or availing any product or service is done online, which is a big hit with Gen Z customers and millennials. Adopting BaaS and reinventing themselves is the best way for traditional banks looking to counter these new players. India's largest bank in terms of branches and customers, State Bank of India (SBI), decided to present itself as a youthful new brand with a campaign titled 'YONO' (You Only Need One). YONO works as an integrated digital banking platform, which allows SBI YONO customers to purchase flight, train, and bus tickets, book cabs, shop online, and pay their medical bills with ease. IBM worked as the solution provider to design, deploy, and launch YONO for SBI.

Other key observations made during the session were about the growing interest among traditional banks to invest in fintech startups and fostering dedicated tech teams within the bank to develop and monetize APIs. BaaS will see a shift from a vertical stack-based ecosystem to a dis-aggregated banking ecosystem. Each constituent in the entire process will focus only on a single task of their specialization. With its focus on 'Open Banking', Australia is passing regulations that make banking much easier. Any authorized service provider will be able to process 'KYC' – a key part of opening new bank accounts.

A word of caution about BaaS – *"The weakest link in the ecosystem can impact the bank/service-provider."* It is akin to one having a bad experience with an UBER driver and then blaming the brand/company on social media. So, reputation management will also come into play.

The key outcomes from the session on BaaS are as follows:

- Regulations and laws passed by governments influence BaaS adoption.
- The onus of providing a frictionless experience to the customer is on the service provider/retailer.
- BaaS adoption and deployment is predominant among banks looking to venture into new markets.
- Banks are pushed to the background as implementation partners and retailers remain at the forefront in a BaaS engagement.
- Not every bank will venture into BaaS.
- Technology is an enabler and more banks are likely to invest or partner with fintechs.

The session concluded with a note on changes needed in regulatory requirements and clear transparent banking policies to facilitate BaaS easily.

About SunTec

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