Alacriti

Digital Transformation: More Than Technology and More Important Than Ever

With the global pandemic redefining normality, digital transformation projects have moved front and center, if they weren't already there. Financial institutions seeking to modernize their infrastructures — with payments as a foundation — hope to improve the consumer experience by meeting rapidly increasing expectations for access, convenience, and functionality. But what does "digital transformation" really mean, and what are the possibilities available by embracing it?

Defining Digital Transformation

CEOs from financial institutions of all sizes and from all around the world have been discussing digital transformation for the last decade in dribs and drabs — slowly rolling out the next-generation or evolution of their current digital experiences. However, confusion around the definition of transformation lies in conflating new features and functionality with reimagining the institution from the ground up.

True digital transformation is a paradigm shift involving re-imagining the entire financial institution — its operations, its culture, and the products and services offered — all enabled by technology. At the highest level, it is a convergence of the physical/tangible to digital to non-physical. While technology is certainly the driving force of digital transformation, organizational culture is equally important. One without the other will certainly result in failure. Organizational objectives must be clearly defined and communicated, and everyone from the C-suite to the front line needs to be operating based on those objectives or risk botching digital transformation in a way that may be unrecoverable.

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Technology, Culture, and Out-of-the-Box Thinking

Achieving true culture change that embraces digital transformation means more than just stating your intention and rolling out incremental features and functional improvements. For example, the imminent shift of the legacy payments infrastructure, our batch-based ecosystem, to a real-time one that is always on and always connected. This shift alone will precipitate a need to not only re-engineer our internal processes, but also it will necessitate us to reimagine the products and services we bring to the marketplace.

Most of the products we have today are simply a continuation of the legacy paper-based, pre-digital world. ACH was meant to replace the paper check, and the digital/mobile wallet is a replacement of swiping plastic, which was a replacement for handing over cash at the point of sale. While enhanced features, like new alerts, are continually added, traditional rails are still at the heart of these payment methods.

While each of these advancements was the result of technological evolution — and arguably have improved financial institutions' ability to deliver improved consumer experiences — neither has been taken to their full potential of product idealization due to technology limitations at the core of these solutions.

As financial institutions let go of their more traditional thinking and do more than just modernize their technology infrastructures by truly embracing the equally important cultural shift, they will have free reign to reimagine products and services free from the restraints of an ecosystem that only runs from 9 to 5 each day. We did a great job as an industry working around those restrictions for the past 30 years of the digital age; however, to unlock the next 30 years of innovation, we must rebuild our foundation. Once that happens, the possibilities are truly endless.

"Most of the existing banking technology infrastructure is monolithic and designed for batch-based processing of ACH and wire payments. Enhancing these infrastructures to support end-to-end real-time payment services is a major challenge. It results in a longer time-to-market."

— Manish Gurukula, CEO of Alacriti

Considerations and Ways Financial Institutions May Leverage Digital Transformation

Here are some ways to envision financial institutions' ability to leverage the possibilities available through technological and cultural digital transformation with payments as the foundation, as well as things that will need to be factored into discussions around digital transformation.

THE CLOUD

Cloud computing has been a hot topic with financial institutions in recent years, but in terms of digital transformation and payments, the cloud provides financial institutions and their developers a platform and set of tools to get started quickly and focus on business problems without having to worry about infrastructure investment. It also allows for scalability without the need to justify large capital expenditures for what are as-yet-unknown costs associated with technological transformation (e.g., real-time payment volumes and general payment distributions, artificial intelligence and machine learning, additional computing power, and the redistribution of the traditional and digital channel mix in a post-COVID-19 world).

The cloud is also facilitating more agile software development. Continual development is increasingly becoming the norm but has been slower to take hold in the world of FinTech, where vendors still tend to stick with rigid release cycles and a pre-defined cadence.

Increasingly, however, the cloud and its continued adoption within banking will allow for more continuous deployment of application updates and fixes, but financial institutions will need to consider who owns what and where the handoff to the financial institution should occur when planning for digital transformation.

Cloud banking also has profound implications for reducing technology debt. Currently, around 70 percent of IT spend goes to maintaining current applications. Continually building on top of existing applications in an attempt to keep up with the latest innovations will only make it increase. For example, as billions of mobile devices around the world may initiate payments, how can a financial institution's supporting infrastructure keep up? The answer is cloud computing, which allows financial institutions to take advantage of the latest technology innovations without adding to existing infrastructure – for a much more nominal cost. It also frees them from the constraints imposed by existing architecture, meaning the sky's the limit for product development and innovation.

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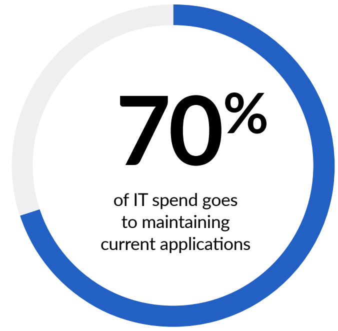


MICRO-SERVICE-DRIVEN ARCHITECTURE

Siloed applications that run independently of one another, or loosely integrate with others in order to perform a specific function while still requiring the whole application to be deployed and running, is an unnecessary inefficiency. Instead, micro-service-driven architecture unlocks the ability to leverage multiple services from various applications or systems seamlessly, only invoking the workflow needed without needing to leverage and run the entire application.

Micro-services allow rapid and simpler deployment of new and better workflows without concerns for the cost-prohibitive nature of implementing new entire systems or products. It changes the decision-making focus from "what's best" to "what's possible with what we have". Currently, the Banking Industry Architecture Network (BIAN) is working on interoperability standards to help make this the norm rather than the exception and enable a build once, use many times approach that developers are looking for.

OPEN BANKING

Open banking through application program interfaces (APIs) is a key enabler of digital transformation. In the past, innovation was held captive by a 2-times-per-year release schedule. Now, open APIs provide unprecedented access to data and applications that can be leveraged by internal or third-party programmers to offer competitively differentiating customer experiences, products and services, as well as roll out innovations on a more real-time basis.

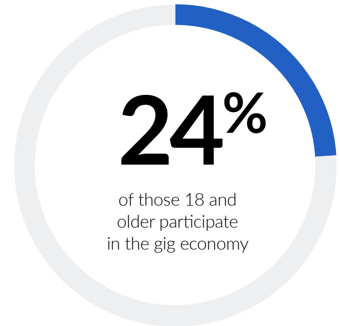
In addition to internal or one-off development, open APIs will facilitate "centers for innovation" where the best minds from within your financial institution – as well as within the banking industry at large – gather to solve common and complex problems.

Financial institutions will be able to benefit from cross-industry innovation and the ability to create unique value-added product packages. For example, combining traditional banking products and services,with retail or restaurant perks, or new subscription-based offerings. It's like expanding value-added credit card perks across your entire portfolio.

The takeaway with regard to open banking is that it can only be fully leveraged if your organizational culture allows you to re-think what's possible in delivering the best consumer experience, end-to-end, while maximizing your competitive advantage.

MILLENNIALS AND GEN Z BANKING

Currently, 24 percent of those 18 and older participate in the gig economy, according to Edison Research, so it's probably time to rethink the weekly, bi-weekly, or monthly paycheck model.



Gig workers don't hold traditional 9 to 5 workdays, they aren't on a set hourly pay scale, and each "job" is done in anything from three minutes to a few hours. This real-time, anytime workforce model doesn't mesh well with current, legacy-based batch processes that take 1-3 days to fulfill. If the consumer's experience as an Uber passenger is instantaneous and painless in terms of payment, why should drivers be stuck held to payments at a certain limited frequency? Uber has responded to this challenge using a "push to debit" system to instantly pay drivers, so funds are available multiple times a day and as they are available.

But why should this stop at the gig economy? There are plenty of industries and entry-level positions that would benefit greatly from breaking the old bi-weekly or 2x monthly paycheck model. Giving businesses and workers options to suit their individual needs is something our new payments ecosystem can support, so it's only a matter of time before the products and use cases start being solved.

Rethinking banking to create new products that make sense to this generation of consumers (and this is very much a generational banking issue) is going to define the future viability of institution-based banking, and can include any number of things like credit scoring using new, meaningful criteria such as social media inputs, innovative ways to make rent payments, ideas to help with student debt, and more. The financial institutions that identify the use cases early and create products for them rapidly stand to benefit greatly as this demographic matures and makes up a larger and larger portion of the workforce.

Digital Payments as the Foundation of Banking's Future

Building your digital transformation using digital payment innovations as the foundation opens up a new world of innovation at a time where competitive advantage is essential to not only surviving but thriving, now and into the not-too-distant future.

Digital payments can be the catalyst for some of these innovations:

- Increased alternative channel adoption, like messaging apps or social media platforms, for example, where an increasing number of tech-savvy users want to pay in a seamless way embedded in the same platform used for shopping.
- Creation of Buying Experiences versus Payment Experiences
- Leveraging AI technology to support alternative channels to accept voice or text payment requests and answer FAQs
- Using QR codes for instant payments or donations
- Solving the problem of how to make digital payments more inclusive and accessible to the un/under-banked (bringing technology down-market)
- Modernizing bill payment platforms for faster/instant turnaround time.
- Making more payment options available on any channel the consumer prefers.
- Make faster decisions with better analysis and reporting of billing history and payment behavior when more payments are digital
- Machine to machine payments, like your car independently paying for gas or parking

As consumers — and the industry — continue to find their way in this rapidly changing and unexpected landscape, we can expect to see much more discussion on digital transformation, as well as real-time payments, which are both poised to barrel into financial institution's strategies for the foreseeable future.

What may seem at first like simply an expense-line item or a nice-to-have can actually help ensure your financial institution's future for years to come. If you haven't already been thinking of how you can transform your financial institution's future through cultural change and digital transformation, the time is now to begin strategizing.