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Virtual Banking in HK: More Hype than Impact?

The Hong Kong Monetary Authority in late August announced it had received 29 applications for its first virtual bank licences, with the applicants ranging from telecommunications operators and financial technology companies to global banks. Hubbis assembled a group of experts at the Digital Wealth Asia Forum to discuss the implications for the wealth management industry.

These were the topics discussed:

- *What customer experience are clients looking for?*
- *Can new banks be successful? Are they really any different? What is actually digital?*
- *How will this evolve in Hong Kong?*
- *Do people see a positive commercial effect? Will anyone make money and how?*
- *Are payments a problem?*
- *Is the cost of delivering financial advice and services reduced?*
- *How will clients transact, monitor portfolios, absorb investment ideas?*
- *Are traditional wealth managers struggling to keep up with client expectations?*

PANEL SPEAKERS

- **Michael Benz, Senior Advisor/Digital Banking, Synpulse**
- **Gary Ng, Partner, Risk Assurance, PwC**
- **Silvio Struebi, Partner, Simon-Kucher & Partners**
- **Ricardo Wenzel, Director, KPMG**
- **Jacob Wai, Chief Risk Officer, MoneySQ**

hubbis

EXECUTIVE SUMMARY

Virtual banking in Hong Kong on the cusp

The HKMA is analysing the applications for virtual bank licenses in Hong Kong, with big domestic and mainland China names having thrown their hats in the ring. A key component of the decisions to award licenses will be the business model, the investment and of course regulation, especially how applicants will manage their risk exposures to ensure financial stability for the customers and for the financial system.

Retail-focused, but SMEs in mind

The target market for the virtual banks is largely retail, as well as smaller companies and SMEs. The rapid onboarding process to be available at the virtual banks will help propel them into the marketplace. Faster turnaround times for everything, including complaints, will also help boost competitive advantage.

Regulation - a net that spreads ever wider

Regulatory oversight of the virtual banks will be as tough as for the traditional banks, and probably even tougher, as the HKMA will want to ensure there are no calamities and because 100% digital opens the door wider to cyber-crime.

Transparency

A panel member cited the disadvantages of the traditional bank, such as non-transparent levying of fees, the annoyance of visiting a bank branch, the slow response to queries on the help desk, and the fact that the banks often ignore some of the smaller clients, even the smaller businesses.

And the aim is? To make money

To make money from these new ventures, the virtual banks must establish transparency, trust and their brands. If they can achieve those elements, then they can build scale, at which point they will be able to monetise their business models.

If you can't beat them, join them...

Some of the local and regional mainstream banking names have their hats in the ring. Why? Because they want to compete in this new banking arena. And because they want to learn by direct experience what it takes to become a purely digital operation, which might be the "bank" of the future.

Seeking out the well-to-do

Wealth management traditionally focuses on the HNWIs, with at least several million US dollars equivalent to invest. But there is a large market of well-to-do locals and foreigner in Hong Kong that would benefit from the focus of the virtual banks on their wealth management needs.

THE HKMA BEGAN ACCEPTING applications in May 2018 for the licences which will enable banks to operate online in the city without physical branches. According to news reports in late August, confirmed applicants included Standard Chartered Bank, online lender WeLab, a consortium led by CASH Financial Services Group, and Zhong An Bank allied with China Citic Bank. In addition, HKT, a joint venture by Bank of East Asia, Airwallex and Sequoia Capital China, also submitted an application.

The idea is that the virtual bank format will help the 'banks' capture new customers. The virtual bank model will use new technology to serve small and medium sized corporate customers as well as individuals who are now underserved by traditional banks.

It is thought that the HKMA will assess how applicants will manage their risk exposures to ensure financial stability for the customers and for the financial system.

Retail-focused, but SMEs in mind

"My first observation," said one panellist, "is that the implications for this development are retail-oriented and will have little impact on the wealth management sector. Retail banking in Hong Kong is dominated still be only a few major names, who are hugely profitable, so I certainly believe there is a lot of opportunity for virtual banks to start addressing some pain points which the normal retail banking client in Hong Kong is facing."

MICHAEL BENZ
Synpulse

SILVIO STRUEBI
Simon-Kucher & Partners

Another expert noted that a key difference between virtual banking and digital banking with a major 'physical' bank is the onboarding process. The virtual banks will be able to offer operational efficiency and seamless, rapid onboarding experience than even the digital arms of the retail banks can offer."

Regulations the same, but 'virtual' faster

"From a regulatory standpoint there is no difference," another guest reported. "Just as with any other bank they must fulfil exactly the same regulatory and other requirements, perhaps more in the sense that the technology risk assessment requirements are higher. Instead of robbers, potentially, there are hackers."

"It is the business model that is different from the traditional banks," opined another panellist. "The virtual bank will have many more data points that a traditional bank cannot capture, and then how they can apply AI technology and to leverage that data."

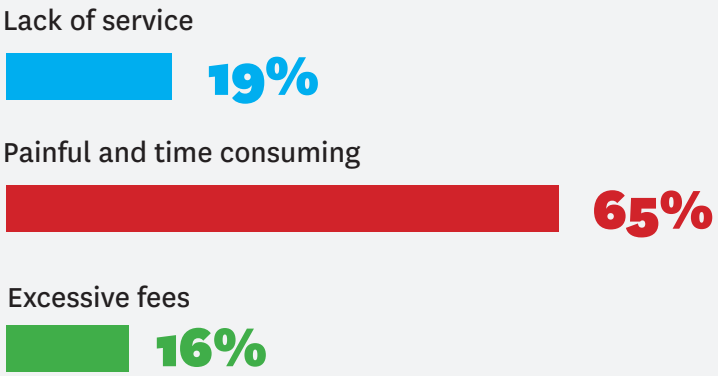
A panel member cited the disadvantages of the traditional bank, such as non-transparent levying of fees, the annoyance of visiting a bank branch, the slow response to queries on the help desk, and the fact that the banks often ignore some of the smaller clients, even the smaller businesses.

Plugging the gaps

"Look at all these rather dissatisfactory elements

RICARDO WENZEL
KPMG

WHAT DO YOU DISLIKE MOST ABOUT YOUR RETAIL BANK?



Source: Digital Wealth Asia Forum 2018 - Hong Kong

and there is a clear opportunity for somebody to come in and find the meaning for a customer," he remarked. Will it be easy? No, as competition will be fierce. Secondly, the HKMA will impose conditions, as well as the same regulatory and reporting requirements, possibly even more."

Another guest suggested that focusing solely on Hong Kong will not be enough for these new virtual banks. "The China angle would be challenging because there are incumbent domestic players which have a very large market share and are very advanced," he noted. "Perhaps elsewhere in Asia there are opportunities for client acquisition. Another factor is access so that clients using the virtual bank can make payments to merchants, to individuals, across as many entities as possible."

An applicant interjected, stating that he believes there is great opportunity, otherwise his own business group would not have applied.

GARY NG
PwC

Opportunity awaits

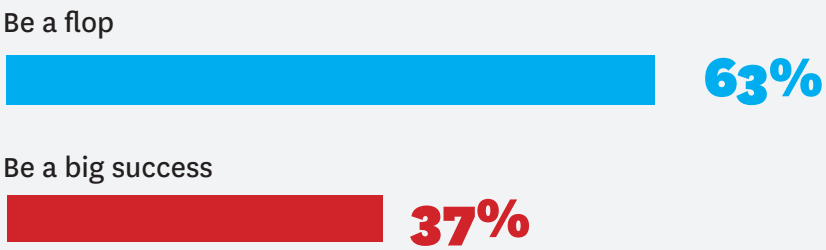
"The regulator," he said, "has already told the market what the target segment is for the virtual banks, for financial inclusion, so retail market and SMEs. For example, it is not easy to set up SME bank accounts, especially for foreigners, but the HKMA wants more focus on these areas, including providing financing; this is an area that has been lacking in Hong Kong. We must look at areas the traditional banks have neglected, and once you look into that untapped market, it is huge."

As to making money from this initiative, a monetisation and pricing expert observed that the applicants, if successful, must build a brand and trust, then scale.

"THE BACKBONE OF OUR BUSINESS MODEL IS NOT ONLY OUR PAYMENTS BUT OUR CROSS SELLING,"

"The backbone of our business model is not only our payments but our cross selling," said one expert. "It probably starts with payments but then it could be insurance, it could be in-depth cross

WILL VIRTUAL BANKING IN HONG KONG



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selling. There are additional revenue streams, so if we build a large client base and good customer relationships, leverage access to data, there are great opportunities."

Seeking agility

Another guest noted that the major traditional banks that are entering the virtual market hope to do so to become more agile in terms of doing business innovatively and cost-effectively, rather than solely following the traditional complex organisational framework. "A new wave will take over the traditional banking business," that is what they are thinking and therefore why they are positioning themselves in the market."

"My overall assessment," stated one expert, is the mainstream retail banks have done a reasonable nice job of digital adoption and transformation, but fundamentally I actually see a very different angle and purpose behind all the virtual bank initiative - the traditional players can establish a virtual bank in a separate ring fenced set up, and thereby all the large banks can actually plan and learn what it means purer digitalised bank."

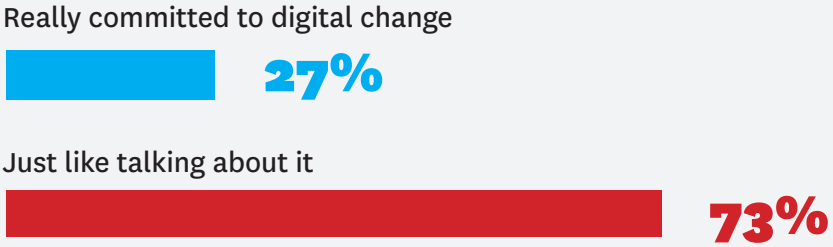
In terms of the business model, he noted that the population in Hong Kong is small with just seven million potential customers, but with many banks, of which about 22 are locally incorporated, retail banking networks. "How will they survive in such as small market?" pondered one panellist. "That is why they strive to be innovative in terms of offering products and building an ecosystem where they partner with certain service providers or even a full online, open API platform to connect with the others, to enhance the client acquisition. And aim to reach the customer using more data analytics and AI to really tap into the service offering that they have not yet explored."

JACOB WAI
MoneySQ

Seeking the well-to-do 'mid-market' clients

Another expert added that in wealth management terms there is a swathe of customers below the HNWIs who are not being well taken care of and who would benefit from more sophistication and guidance and access to maintain and accumulate their wealth. "That will be in the future business model of the virtual banks," he said. ■

ARE WEALTH MANAGERS ..



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