

Pursuing Mobile Banking Solutions

By George Simotas, Joel O'Driscoll and Josh Linder

Mobile banking continues to receive increased media attention in the U.S. market. However, the path for many banks to successfully pursue a mobile banking strategy and supporting solutions is still unclear. Some of the key issues that banks must address to pursue mobile banking include:

1. What are the strategic objectives for mobile banking?
2. What have been the most successful business models for mobile banking?
3. What are some of the most important considerations related to implementing a mobile banking strategy?

This article aims to provide some insights around each of these questions that may be helpful in developing or refining a mobile banking strategy.

1. Objectives for Offering Mobile Banking

Today, financial institutions offering mobile banking services typically do so to satisfy one or more of these three key objectives:

- **Attract or grow a customer segment** -- deliver new and existing services via mobile devices to new and existing customer segments who value more convenient ways to access their accounts
- **Capture economic benefits** -- reduce the cost of delivering customer service over more expensive channels that involve personnel, such as those in branches and call centers
- **Increase retention** -- personalize marketing messages and communications that enhance the brand and increase loyalty and retention

Customer Segment

In the U.S. market, mobile banking has experienced greatest adoption among the customer segment known as the "Millennial Generation" (aged 18 to 34). This is the first generation to grow up with widespread availability of mobile phones. Millennials are generally very comfortable using new technology and enjoy the convenience of using mobile phones as more than a mere communication device. They are also more likely than other age groups to use a mobile phone for micro transactions such as purchasing ring tones, music, and mobile applications. As the need for banking services increases among this segment, they are far more likely to be early adopters of mobile banking. As such, they represent a good initial target segment for mobile banking services.

Economic Benefits

A 2009 study that compares transaction costs across delivery channel concludes that mobile is the least expensive channel to service customers (See Fig. 2).

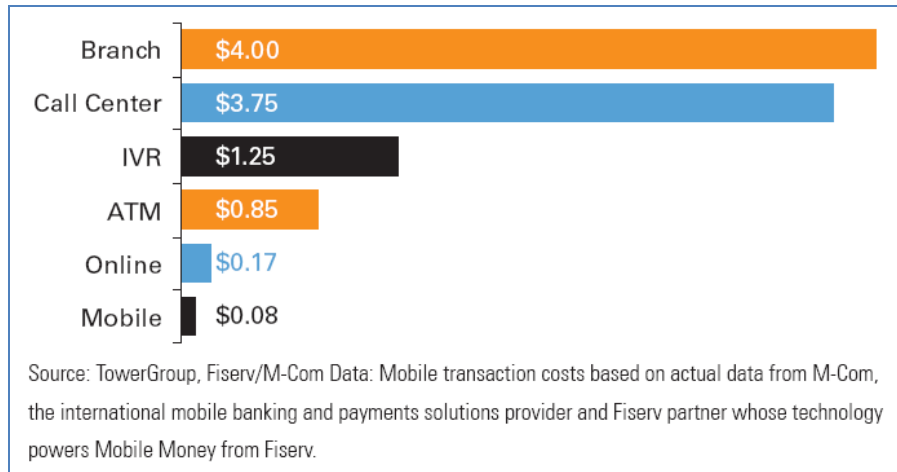


Fig. 2

On the surface it might appear that the most logical customers to migrate to mobile banking would be those currently using online banking. However, online banking is the second least costly servicing channel. Thus, financial institutions seeking to increase their ROI from implementing mobile banking solutions should consider migrating customers away from branches, call centers, and IVRs to mobile banking. Doing so will likely require innovative incentives, education (around security, for example) and/or product packaging. However, the payback is potentially large and immediate.

Retention

Providing value-added, differentiated services is one driver of customer retention. For example, many consumers are looking for ways to track and manage spending, particularly in these difficult economic times. The 2010 Hitachi Consulting/BAI Study of Consumer Payment Preferences found that financial control (managing a budget and spending) is important – and equally important across all age groups (See Fig. 3) -- when selecting one payment method over another. Financial institutions can provide a valuable service by offering capabilities that are beneficial to consumers seeking these services.

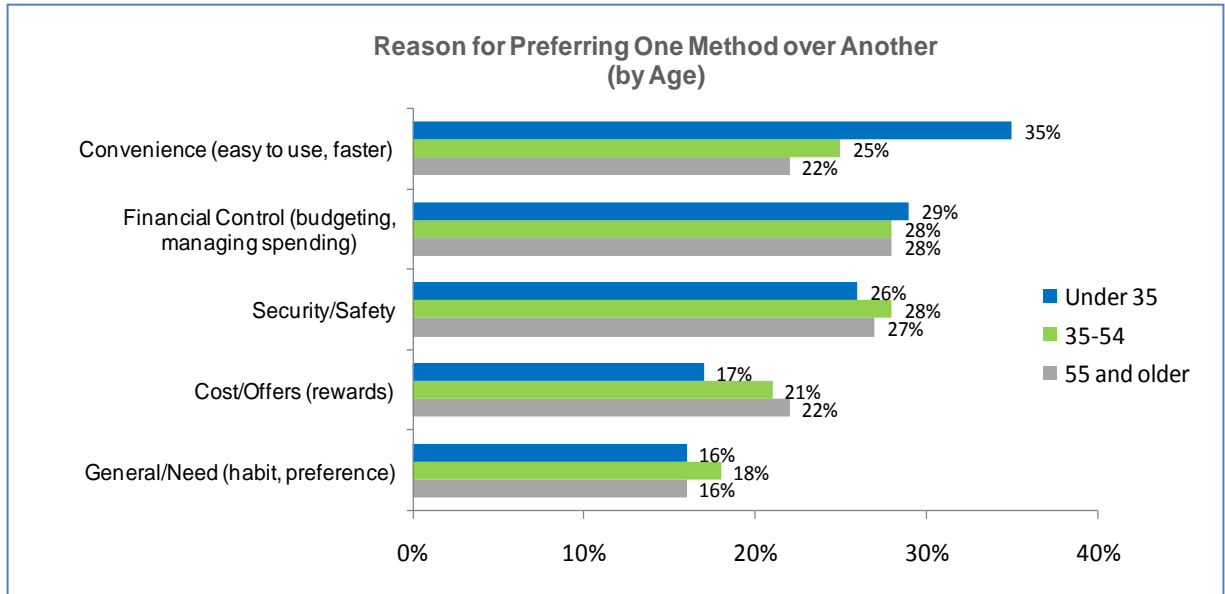


Fig. 3

SMS alerts on a mobile phone can provide consumers with account balance updates that can help them manage their spending and control their finances on a timely, if not real-time, basis. SMS messages can also be used to alert customers about potential fraudulent transactions. With today's heightened public awareness about identity theft, offering fraud alerts via the mobile channel demonstrates that financial institutions are helping customers manage their risk of identity theft.

2. Mobile Banking Business Model

Two business models exist for mobile banking as it relates to channels: 1) treating mobile banking as a separate channel; 2) integrating it with other channels. The chart in Figure 2 reflects the transaction cost differentials between the different forms of servicing customers. However, that chart does not reflect the potential benefits of having both a common, consistent customer experience across all channels/contact points and information that is consistent and synchronized regardless of access method. For example, if a customer were to open an account, make a deposit in a branch and be able to make a transfer later that day using a mobile phone, that customer would perceive tremendous value. Implementing this would require the account opening and deposit processes to be synchronized with the mobile banking channel. Wells Fargo was one of the first large banks to introduce this capability. This integrated model provides a potentially superior business model for banks that treating mobile banking as a separate channel.

3. Implementation Considerations

There are a number of implementation considerations that financial institutions should take into account when developing a mobile strategy. They include:

- Services to be offered
- Vendor risk management
- Regulatory compliance

Services to be Offered

Many financial institutions that provide mobile banking offer one or more of the following services:

- Locations of branches and ATMs
- Transaction alerts
- Account balance and transaction inquiries
- Money transfers between accounts and with third parties
- Bill payment

Additionally, solutions for contactless payments are being developed and piloted by financial institutions, card associations and solution providers.

Financial institutions need to understand their target consumers and how they want to have their banking services provided. Implementation of mobile banking may take a path similar to that of ATMs which, when first introduced, had limited functionality and required a tremendous amount of education to gain adoption. Pursuing a phased implementation may limit initial investments and would allow for providing additional value-added services as consumers become more familiar with mobile banking.

Vendor Risk Management

Financial institutions will need to consider the operational risks presented by vendors who provide mobile banking-related services to them as part of their third party risk management practices.

Potential risks include those resulting from:

- Fraud
- Errors and omissions
- Failure to deliver products or services
- Failure to comply with legal and regulatory requirements that govern the delivery of financial services

Financial institutions will need to revise their vendor risk management process to be able to quickly identify, measure, monitor and control these operational risks.

Regulatory Compliance

One of the major concerns about mobile banking relates to regulatory compliance. Banks have been viewed as a trusted agent when it comes to executing safe and secure financial transactions. With the

introduction of a mobile carrier between the customer and the bank, a range of new legal, regulatory and operational issues arise.

For example, financial and reputational risks can arise if financial account data is compromised due to a breach in security “over the air” or at a mobile carrier’s data center or if a transaction fails to be completed. Issues regarding assigning responsibility for losses and determining what contractual obligations may be required will need to be negotiated between financial institutions and mobile carriers. Financial institutions will need to review how the relationship with mobile carriers will impact and be integrated into its risk management practices as they relate to complying with their own security procedures and Regulation E processes.

Risk exposure may also arise from Bank Secrecy Act and Know Your Customer considerations. The challenge may come from a new wrinkle in being able to accurately determine the identity of an existing customer. For example, changes in customer agreements and disclosures, and screening and authentication processes may be necessary to confirm that customers using mobile banking are in compliance with these regulations. Changes in customer agreements and disclosures may also be necessary to limit a financial institution’s liability to a failed transaction that occurs outside of its control. The above items represent merely some of the risk management considerations that banks may need to address in implementing a mobile banking strategy and they should seek legal counsel to identify applicable risks within their organizations.

In Conclusion

While mobile banking has received increasing hype in the U.S., its development has been slower here than in Asia and Europe. Nonetheless, mobile banking in the U.S. finally appears to be gaining traction, albeit slowly.

As we have described in this article, how your bank thinks about mobile banking involves more complexity than merely adding a mobile banking capability or channel. Strategic objectives need to be defined. These objectives, in turn, have implications for numerous other areas of the bank, including segmentation of customer segmentation, development or refinement of sales and service delivery models and investment in enabling technology, to name a few. The outcomes of these decisions, in turn, have further consequences related to business economics, regulatory compliance and risk identification and mitigation.

Hitachi Consulting can help you to address these important issues and develop or refine your mobile banking strategy. We look forward to meeting with you.

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