



# Digital Banking

## **A new business opportunity in Malaysia?**

Key winning theme  
– Customer-value concept



KPMG in Malaysia

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# Customer centricity is key for a successful digital banking business in Malaysia

**M**any companies and entities in Malaysia are more open and ready now to have active conversations in the market to explore a new business opportunity, “digital banking”, post COVID-19. The current pandemic has forced businesses to shift from the traditional way of doing business, instead embracing digital transformation to provide products and services online thus bringing their offerings directly to the customers.

In addition, a new consumer is emerging globally – one that is more advanced in their use of digital technologies and more thoughtful and selective in their decision-making. It is becoming more important for organizations including banks to focus on digital enablement of their customers and be clear on where they need to win customer trust. Digital banks can be the main beneficiaries through focusing on customer value propositions such as value for money, ease of use and digital security.

## The Malaysian landscape so far

Bank Negara Malaysia (BNM) had issued the Policy Document on Licensing Framework for Digital Banks (Policy Document) on 31 December 2020 following a six-month public consultation through its exposure draft. The issuance acts as part of BNM's commitment in facilitating innovation for financial services in Malaysia.

BNM had emphasized in its Policy Document that digital banks in Malaysia are required to demonstrate commitment to driving financial inclusion, particularly to the underserved and unserved segments. In its frequently asked questions (FAQ) of the Policy Document, BNM had defined unserved and underserved segments as a group of individuals and businesses whose needs for financial products and services are not adequately served or met.

The definition was further broken into 3 categories which are:

- Customers who face challenges in obtaining financial services due to higher information asymmetry and higher risk profile. For example start-ups, SMEs with insufficient collateral, self-employed individuals, first-time borrowers, individuals who recently joined the workforce and retirees;
- Customers with low level of financial literacy; and
- Customer segments that are physically difficult to reach or be served through traditional means.

With the submission date set to 30 June 2021, many interested applicants will need to start the application process and focus on meeting the requirements of BNM. Other areas highlighted concerns the use of transformative technology which is expected to deliver better financial services to customers and build robust risk

management and compliance capabilities to meet all the required regulatory requirements from all the relevant regulators.



It will be interesting times to come as there will be many developments in the market as more parties join the conversation and the increase in announcements relating to consortium formation is expected.

Currently, many interested applicants in Malaysia prefer to form a consortium instead of being a sole applicant. This model is quite common especially in the Asia Pacific region. Some examples of digital banking consortiums include Airstar Bank, Mox Bank and Fusion Bank. The companies that are part of the consortiums are often from a wide range of industries such as traditional banks, insurance companies, property developers, telecommunications and technology companies locally and abroad.



# Customer-value concept

A successful digital bank is a bank that a customer can trust. This means having a customer-first mindset, being able to target the right segments, provide them with confidence in its banking operations, and keep them continuously engaged within the bank's platform. The path to profitability will be based on volume-game for digital banks. This is mainly driven by BNM's objective to promote financial inclusion and improve the country's financial literacy index as stipulated under section 7.2 of the Policy Document. Competition will be strife, and margins will be thin given the need to offer competitive pricing for these segments.

In addition, under section 13.1 of the Policy Document, there is a key business restriction that the total size of assets cannot be greater than RM3 billion at any given point during the foundational phase. This ceiling hinders the banks from focusing its services on niche or small groups of customers, as concentration risk will then arise.

As such, digital banks need to have continuous deep analytics of customer behavior and needs. Flexible product features can be enabled to provide a range of services to the customers based on their needs. Examples include "bite-sized" service offerings, flexible withdrawals, tenures, repayments for the products offered. This will help optimize the permissible asset size, and manage customer engagement better.

A digital bank with appropriate technology capabilities will be able to deploy these products to a large customer base, given the more advanced and agile technology digital banks typically function on.

The customer-value concept is divided into 3 key themes:



## i. Customer Centricity

To understand how digital banks can differentiate themselves and attract new customers, they must first identify the market gaps and understand the different customer segments' pain points at each phase of the customer lifecycle. Based on BNM's preliminary view of Malaysia's financial services offerings, there are still huge gaps in insurance and takaful products, of which the total premium to GDP is only about 4.7% (Thailand: 5.0%). This is followed by market opportunities in micro SME lending, e-payments and asset management space. However, the banking penetration in the retail segment in Malaysia is actually relatively high with only 4% of the unbanked population as government payouts and salary are distributed through personal bank accounts especially before e-Wallet players come into the picture.

Does this mean that the Malaysian market for financial services is already saturated? How does a new digital bank become profitable given the small population base in Malaysia? And how can the bank increase its customer base?

In addressing these challenges, digital banks must go beyond what the traditional banks are currently offering and be agile to any possibilities. With Malaysia's digital acceleration agenda and BNM's acceptance towards open banking, it enables digital banks to offer holistic solutions covering both financial and non-financial services in one platform to the unserved and underserved segments through wider market reach and more availability of data to assess credit risk.

The target segments for digital banks in Malaysia can be broken into 2 main categories; (a) retail market and (b) SME market.

### a. Retail market

Malaysia has a population of 32.7 million as of June 2020, and is among the top 50 most populous countries. Interested parties should not be worried about the Malaysian market size given that digital banks have been operating in countries with lower population size such as Australia, Singapore, Hong Kong and Switzerland.

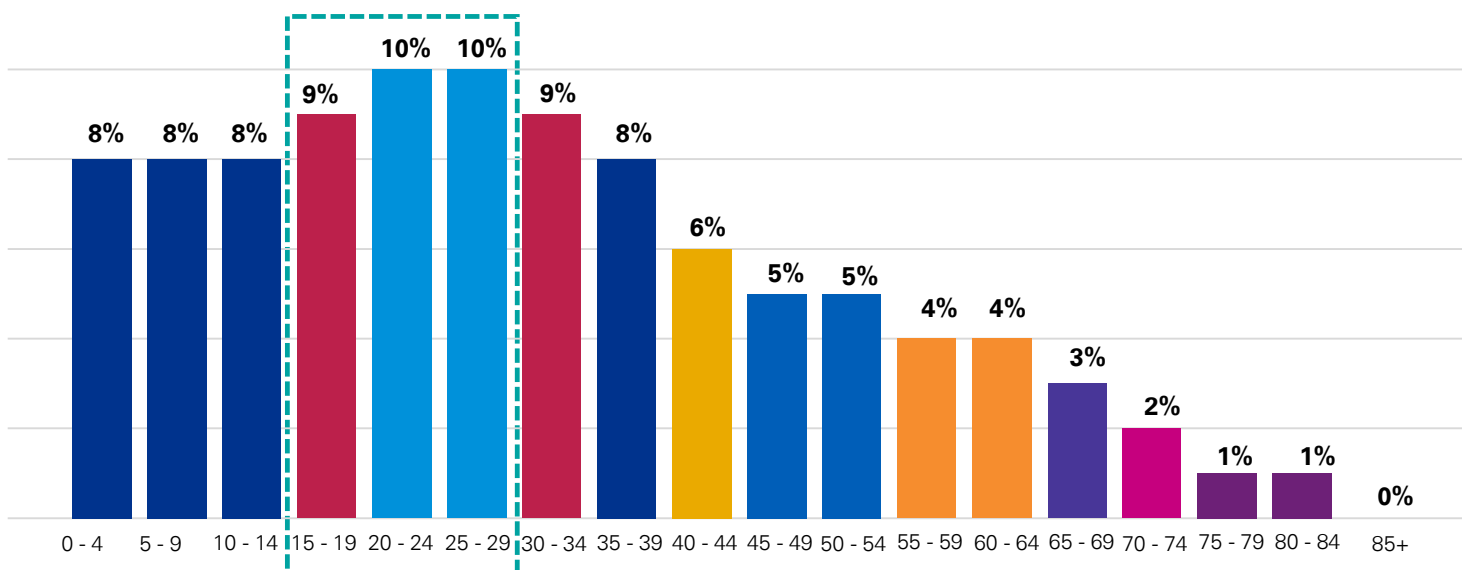


As of 2019, 27% of Malaysians are part of the rural population, while 29% are youths aged between 15 to 29 years old. The median household income in rural areas is RM3,828 (Urban: RM6,561). Almost 30.3% of households earn less than RM4,000 per month and 17.3% have sources of income coming from self-employment. A large portion of these categories fall within the unserved and underserved segments.

Other potential market segments are foreign workers and international students residing in Malaysia and require at least a channel to receive cash, make payments and transfer money in and out from their origin countries. There are about 3.1 million non-citizens in Malaysia as of 2019. We can see an increasing trend of foreign workers' remittance outflows over the last 5 year period, where the transacted value is around RM29.2 billion in 2018. These are mainly payments made to Indonesia, Bangladesh and Nepal. There are about 89.4k international students studying in both private and public universities in Malaysia.

Customers are looking for affordable products and services, as well as simplicity and transparency, when deciding to sign up for an account opening rather than the type and number of products being offered by a financial services provider. It is crucial for a bank to understand each segment carefully given that there are different levels of awareness, expectations, challenges, digital proficiency and education for each individuals. As such, a customized approach is needed to successfully attract them to onboard the digital banking platform.

### Malaysia largest population category is the youth segment, aged between 15 to 29 years old, a group that is mostly tech-savvy and trust tech giants



Source: DOSM, Population estimates as at 2Q 2020 by age group

As an example, Kakao Bank had successfully grown its customer base to more than 10 million (20% of Korea total population) in two years since it began operations in July 2017. They receive about 14,000 new customers daily. Kakao was originally a dominant mobile messaging app with a strong warm base, thus making it easier and cheaper for the Bank to onboard these customers. The Bank has not yet open its services to foreigners as the Korean government’s system can only accept local registration cards as a form of an ID when opening an account through a digital platform. A large portion of its customer base is in their 20s, followed by those in their 30s and 40s. Kakao also has over 200,000 customers aged 60 and above.

Similarly, a majority of the customer base for Up Bank is between 20-28 with the top age being 21 years old, a segment that trust tech giants over banks. Millennials aged between 18-36 years old make up about 24% of the Australian total population. This shows that the customer base for many global digital banks is mainly the youth segment, of which digital banks in Malaysia would also have similar customer demographic profile.

Based on results of a survey conducted by Forrester Analytics in 2020, Covid-19 has elevated the importance of financial well-being. There are 75% of Malaysians, median age of 35 years old, that have opened an account with a new financial provider that can help them improve their financial position. There are also customers who are willing to transfer out all their salary into another bank that provides better services such as customer analytics. These show that customers are prepared to switch to another financial provider if they are able to offer more competitive services and better user experiences.



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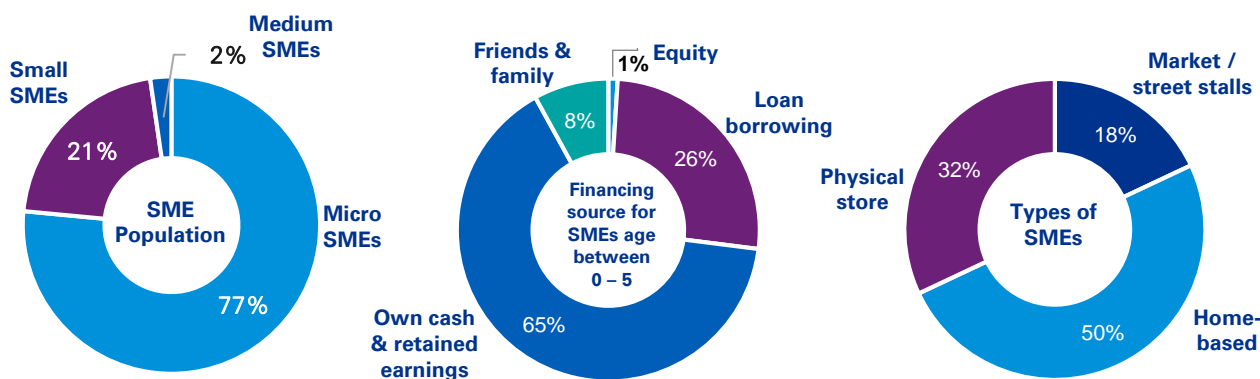
...increasingly we see that user experiences are incredibly important and are really critical in ensuring that you deliver a unify value proposition while also meeting customer expectations. It is no longer just good enough to have a great product, but they are also demanding for better experiences from providers they interact with ...



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- Session 2: Designing a Customer-Centric Bank

**b. SME market – Micro SME and Small SME**

The GDP for Malaysia’s Small and Medium Enterprises (SMEs) grew at 5.8% as at 2019, a higher growth than the country’s GDP of 4.3%. More than 90% of SMEs are small and micro enterprises with only 26% of funding for SMEs with less than 5 years of establishment being from bank loans or financing. A large portion of funding is still coming from own cash and retained earnings that limit the businesses potential growth.



Sources: Department of Statistics Malaysia, Bank Negara Malaysia, World Bank, SME Corp Malaysia

According to a survey conducted by the Institute for Democracy and Economic Affairs (IDEAS) in 2019, the top 3 business challenges for micro and small enterprises are (1) understanding customers; (2) managing cash flow and (3) managing productivity. Moreover, many SMEs find it challenging to digitalize their businesses across the whole spectrum; front, middle and back-end functions. The most common perceptions on why SMEs are reluctant to change their existing business models are due to several factors, namely a lack of awareness on the different digital solutions available in the market, the large effort required for digital transformation, lack of resources and capital investment, high implementation risk and not having the necessary infrastructure, tools or expertise to execute the change.

Based on a survey report on Post RMCO SME Status conducted by SME Association of Malaysia, only 43% of SMEs have embarked on digitizing their businesses and 69% considered their digital transformation journey successful.

In line with Malaysia’s industry revolution 4.0, digital banks can address these gaps by providing financial support and customized business solutions to the segment. Digitalization promotes higher productivity, improves livelihood and may reduce operational and disruption risks from unexpected events such as the current pandemic. Examples of business solutions that are currently being offered by digital banks

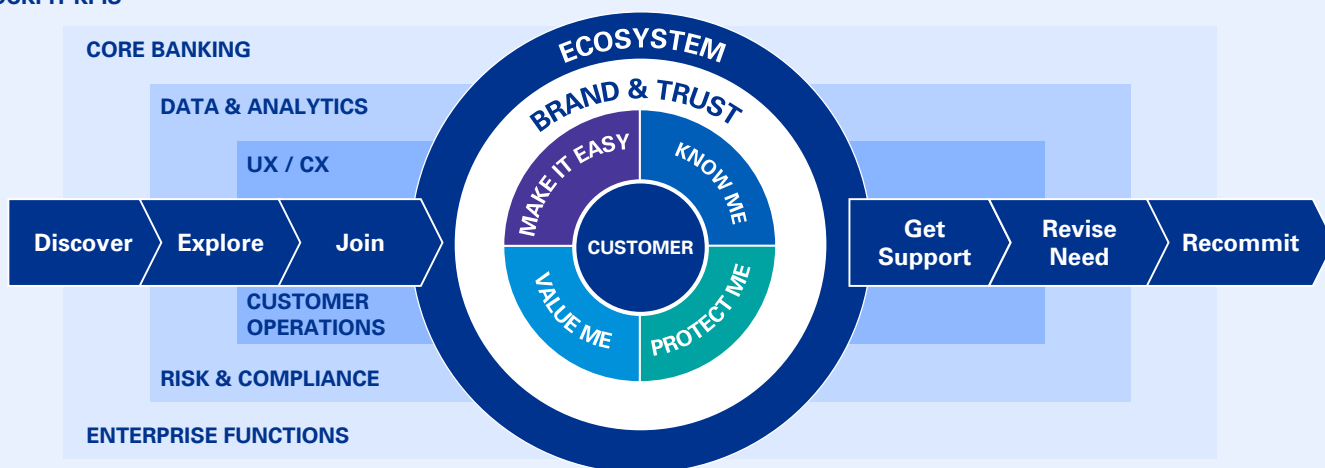
globally include business integration within the banks’ marketplace platform, inventory control and a finance toolkit – bookkeeping, invoicing, tax, accounting services, projected cash flows, working capital and supply chain management.

All customers are valuable to the business. The bank attains value by keeping its existing customer pool continuously engaged within the bank’s platform. Based on BNM’s FAQ on digital banking license application framework, BNM does not restrict digital banks from onboarding customers who fall beyond the unserved and underserved segment. It is a positive signal for digital banks that successfully attract this segment i.e. the services might be on par or better than what incumbent banks currently offer. However, it is important for digital banks to not sway from the primary aim of improving financial inclusion in Malaysia.

## ii. Customer Experience

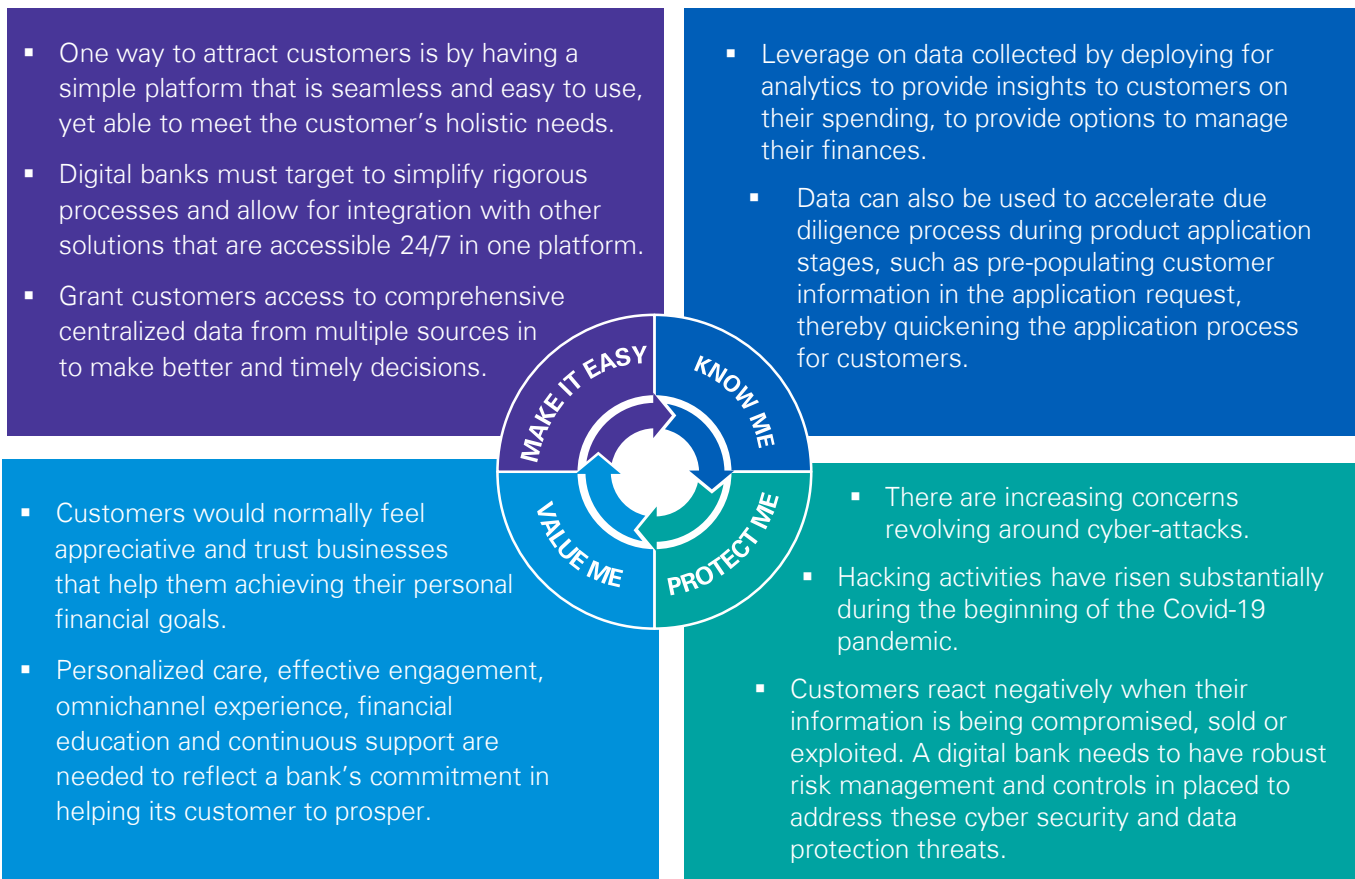
Next, digital banks must design a platform that is able to provide deep, real time understanding of customer behavior and pain points. From there, the banks can start assembling offerings and solutions that they think would deliver the best customer experience and personalized care. Best customer experience can be defined as convenience, quality service and speed. This can be explained further through the diagram below:

### COCKPIT KPIS



Source: KPMG Analysis

Here are 4 key areas to consider when designing a customer centric digital bank with strong customer experience :



One main challenge is that everyone is unique with different needs and level of digital proficiency. Based on the Edelman Trust Barometer, 3 factors that may lead to a reduction in customers’ trust are lack of cost transparency, confusing products and services and unwanted selling. As such, a deep understanding of customers and ecosystem through gathering information from feedbacks, surveys and social media could help to improve a digital bank’s customer experience services. Customer experience must be part of its normal business operating model as this will assist banks to anticipate customers’ needs and subsequently refine their customer experience

model as and when needed. This could help the digital banks to keep the customers retention rate at an acceptable level.

**iii. Customer Capability**

Are digital banks designed and equipped to deliver what we promise to customers? The answer is yes. As digital banks are compelled to show satisfactory progress in fulfilling committed value proposition, they must form a holistic banking solutions and this may be difficult to achieve alone. There are 3 different business operating models that a digital bank can consider:



**Build**

Build own functions and capabilities by utilizing resources its currently own, or are able to procure.



**Buy**

Buy and absorb organizations that have already built the solution.



**Partner**

Partner with other firms to create an offering that is typically greater than the sum of its parts.



Once a digital bank has decided which business operating model to adopt, the bank can start designing its business, technology and operational structure. It must move towards a customer specific model as opposed to product specific and silo framework. With the use of digital technology where most data can be integrated and provides better insights, banks are now able to offer tailor banking solutions to retail and SMEs customers efficiently, effectively and economically. However, at all times, banks must comply with BNM's guideline on responsible financing and not try to mis-sell products and services, as it may expose businesses to legal and reputational risks. As per a quote,



**Trust takes years to build,  
seconds to break, and forever  
to repair. ”**

In most cases, digital banks are built from scratch. It is important to prioritize on what solutions they would like to offer to complement their core business and differentiate themselves from others. They will start small and grow as they gather more market insights on what the gaps are. Some start with focusing on one specific customer segment and grow to another segment, some just offer deposits and lending products then subsequently bring in other products such as insurance and wealth management. The essential part is to have a continuous financial and non-financial product innovation within the bank that are speed to market based on market changes, creative and flexible. Speed to market allows businesses to grow market share with lower cost and less time spent thus higher profitability. Of course, this can only be done by having a strong product team, IT infrastructure and systems that are agile enough to accommodate creation of new products and services.



Another area to focus on is growing the right digital banking ecosystems. Based on MCMC Internet Users Survey 2018, the top 3 online activities for Malaysians are (1) communicate by text; (2) visit social networking platform and (3) to get information. However, consumer behavior can change rapidly. For example during the current pandemic, there is significant increase in online shopping, e-learning, e-sport and online banking activities. Moreover, young generations do prefer renting as compared to owning an asset, opt for 'Buy Now Pay Later' scheme and are willing to pay additional fees for flexible terms and conditions. As a digital bank is building up its ecosystem, the bank must be prepared to make changes. Same goes to its partners, merchants or other third party service providers. There will be a lot of changes throughout the digital banking journey and any disagreement or conduct risk may cause delay in operations, loss of revenue and increase in customer attrition rate. Depending on the type of partnership arrangement, digital banks could bypass middle parties by connecting consumers directly to the providers, making their services cheaper and quicker.

With an open banking concept, it is easier for digital banks to connect and integrate with other platforms when developing their ecosystem. It gains traction and allows banks to deliver on what they promise while creating value for themselves. It enables data sharing across bank and non-bank third-party providers through the use of application programming interfaces (APIs). Most common information shared through open banking includes payment status, transaction initiation, account information, product information and customer insights.

From digital banking users' perspective, Government of Malaysia has come up with the National Digital Network (JENDELA) initiative to improve digital inclusion that looks at accessibility, affordability and application. Based on a report by International Telecommunication

Union 2019, 81.2% of individuals in Malaysia use the internet, compared to a global average of 73.6% across 82 reporting countries. Mobile broadband is preferred over fixed broadband with a penetration rate of 134.5% in 2018 (Singapore: 148.8%; South Korea: 129.7%). The country is targeted to have 96.9% of the populated areas nationwide to be covered by 4G services by 2022 before 5G project takes place. In terms of affordability, the postpaid average price has becoming more competitive over the years as compared to the prepaid plan. Digital banks and users will definitely benefit from government network enablement initiatives.



**Jessica Lam**  
Group Chief Strategy Officer  
WeLab

Key priorities for aspiring digital banks to consider when looking at operating model and implementation of a future-ready bank:



I think one of the most important things is to be agile and prepared to make changes; it's pretty likely that plans will have to change many times along the way. I would also encourage you to have proactive dialogues with your regulators, we found them to be very open-minded and receptive to new concepts and technologies. ”

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- Session 3: Building a Future-Ready Bank

Customer-value concept is key in building a successful digital bank. This can be achieved with strong customer base, seamless customer experience and a robust business structure to deliver customers' needs and boost their level of trust. When customers start trusting a digital bank, it is natural for them to talk about it to their families and friends. This is one of the most effective way for a business to attract new customers as opposed to other advertising channels.

# Is there a business case for digital banking in Malaysia?

Globally, the value of digital banks had doubled when comparing 2019 position against 2018. Many incumbent banks are also starting to embrace emerging technologies and collaborate with fintech companies to remain relevant.

Our KPMG survey on the Malaysian consumers' readiness in digital banking indicates a strong case – 77% with the view that digital banking is the way forward.

Indeed, with a clear business model, right target segments and product offering, the digital bank has a promising opportunity to be part of this evolution.

More specific to the BNM agenda, digital banking will play a role in improving financial inclusion and financial literacy levels of the population. As the unserved and underserved segments become more financially literate and stable, so will their contribution to growing the Malaysian economy.

## How can KPMG help?

At KPMG in Malaysia, we have a ready execution plan that can help you throughout your digital banking journey, starting with licensing. We have had experience in end-to-end digital banking development globally and regionally.

Capabilities that KPMG brings to your organization include:

### Business plan and partnership assessment

- Conduct market feasibility study
- Develop business strategy (covering technology advisory support) and corresponding financial projections
- Perform partnership assessments

### Digital bank license application support

- Assist in preparing application documents
- Review submission documents
- Discussion and responding to BNM

### Independent external review of the business plan

- Review and provide assurance on comprehensiveness of the business plan and pro-forma financial statements

### Operationalization project management services

- Develop project charter including business impact and level of effort, business owners and measurable milestones/metrics
- Core platform technology vendor management
- Advisory services during operationalization

We also have a committed team of financial services professionals and specialists in strategy & partnership, regulatory and compliance, technology, operations, risk management, AML/CFT, governance & sustainability and data analytics that provide comprehensive advisory guidance.

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