



INNOVATIONS IN FINANCIAL SERVICES – A BIRD’S EYE VIEW

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ABSTRACT

Today the contribution of services to the economy is ever growing. Services are characterized by their intangible nature as well as the joint involvement of the producer and the consumer for the service to be enacted. Rapidly advancing technologies, evolving customer expectations and a changing regulatory landscape are opening doors to innovation in financial services. Financial innovation is both complex in character and inherently relevant to economic growth, and full understanding of it requires the collaboration of experts and scholars in many fields of research, including economics, finance, marketing, law and technology. Nevertheless, innovation in financial services remains under investigated and it deserves careful attention, especially since the world is currently going through a period of economic slowdown. Innovation in financial services is very different than innovation in a physical product environment. It is a structural approach that is needed, with a continuous attention to skills development and a multidisciplinary team. Two categories of innovations are – product and process innovations. The former are exemplified by new derivative contracts, new corporate securities or new forms of pooled investment products, while the latter are typified by new means of distributing securities, processing transactions or pricing transactions.

For the financial services industry to be truly sustainable, it needs to practice financial inclusion in embracing online technologies and mobile applications so as to be well placed to ride this emerging trend of digital banking to serve the corporate, mass affluent customers & high net worth individuals at large. This could well represent huge online opportunities for the industry as a whole.

Key Words: Bitcoin, API, Social Media, Open Source, KYC

INTRODUCTION

Rapidly advancing technologies, evolving customer expectations and a changing regulatory landscape are opening doors to innovation in financial services. From crypto-currencies to big data to peer-to-peer lending, fintech innovations have captured the attention and imagination of customers, investors and incumbents. Innovation is important for the survival of every business sector, and financial services are no different. Indeed, research confirms that innovation affects a firm's performance positively. While the vital importance of innovation in today's competitive climate has been widely proclaimed, innovation is not without its challenges. Many such challenges relate to how customers adopt related innovations. It is one thing to innovate, but entirely another for the innovation to be accepted by consumers.

In much of financial services, a "perfect storm" of challenges is leading institutions to embrace new thinking. Heightened regulation, margin compression, declining use of branch networks, asymmetric competitors, and increasing commoditization -- to name just a few factors -- mean that there is real urgency to change.



NEED FOR INNOVATION

There are various ways to foster innovation in a company, it all requires the allocation of people and funds to collect or create new ideas for the company's service provision. This service provision is not limited to the external environment but also involves the company's internal environment. In other words, the concept of "financial innovation" can be defined as making and promoting new financial products and services, developing new processes to facilitate financial activities, to interact with customers and to design new structures for financial institutions. The need for innovation in the financial services industry as a whole cannot be overemphasized. Financial innovation drives the financial system towards the theoretically limiting goals of zero transaction costs and dynamically 'complete' product markets. The ultimate criterion when judging financial innovation is the extent to which it increases the efficiency of financial intermediation; as with innovations in other industries, financial firms can invent a brand new class of products (financial instruments, techniques and markets), modify existing products, or combine the characteristics of several different products, thereby making financial intermediation more efficient. Two categories of innovations are – product and process innovations. The former are exemplified by new derivative contracts, new corporate securities or new forms of pooled investment products, while the latter are typified by new means of distributing securities, processing transactions or pricing transactions.

Financial innovation is both complex in character and inherently relevant to economic growth, and full understanding of it requires the collaboration of experts and scholars in many fields of research, including economics, finance, marketing, law and technology. Nevertheless, innovation in financial services remains under investigated and it deserves careful attention, especially since the world is currently going through a period of economic slowdown. Innovation in financial services requires an interdisciplinary approach. Experts in innovation, management, marketing, economics, business, finance, technology and law need to share their insights to fully foster an open innovation approach in financial services. Bringing together external and internal actors is a key element in fostering an open innovation approach. This can also be applied in financial services innovation.

Innovation in financial services is very different than innovation in a physical product environment. Most innovations can and will be copied by competitors so the search for the "chicken with the golden eggs" is not the best tactic. It is a structural approach that is needed, with a continuous attention to skills development and a multidisciplinary team.

CHANGES IN FINANCIAL SERVICES

Technology has so far made it possible to accelerate the pace and volume of transactions, but it has not transformed the relationship between the industry and its customers in the same way as it has in, (i.e), publishing (from books to e-books), movies (from DVD to mp4), or popular music (from CD to mp3 to streaming).

Next generation of consumers: The Internet is now more than 20 years old, which means that anyone under 40 has never known a social or working life without it. As a result, younger consumers come to the market with different expectations from service providers. Instead of technology being used to hold them captive, they expect service providers to use technology to empower them to determine not only how services will be provided, but what services will be provided. Just consider how today people prefer to use their Facebook name to identify themselves to new sites on the Internet, showing how the power gradually moves into their hands.



People who today have no access to financial services and resort to cash for all transactions: The traditional banking system has all but ignored them, as they don't fit the established business model of the banks. The problem the banks have in serving these people is not so much in terms of lack of revenues, but it is mostly of having access to them, as many of the poor people are far away in rural areas without traditional banking coverage (branches and ATMs). The other problem is getting to know them, as the traditional ways of identifying people (social security, street addresses, etc.) are mostly not available to these people. On the other hand, a large majority of them have a mobile phone, a very powerful instrument of not just communication, but also inclusion. This explains why the telecommunication companies are increasingly seen as instrumental in making financial services available to the unbanked.

Way of accessing consumer financial services: Perhaps this change is most perceptible with the advent of the tablets. The smart phones and especially tablets have simplified this considerably, but most of us are still facing a different app for each service provider, while what we really want is to have a seamless and integrated view of our financial assets. One identity, one user interface for all service providers.

The above changes are driving the pace of technological innovation.

FOUR FINANCIAL INNOVATIONS

The bitcoin: Blockchain, a single database massively distributed and replicated, without any central coordinating point. This is a low cost, worldwide, multi-currency payment mechanism which is faster, more secure and simpler to use than any banking based alternative. The system is based on secure wallets managed by the users themselves, and a distributed ledger inspired by the bitcoin blockchain. From the customer perspective, the operative word is low cost — the system is open, and as there is no central authority necessary, there are therefore no fees associated to intermediaries.

The business API (application programming interface). The API has been used for many years by software developers to assemble program components within an application. The new use of APIs is to make business functions available as components on the Internet. The promise of APIs is to grow volumes from existing customers, and attract new customers without friction. Adopting APIs does require a leap of faith in the traditional marketing doctrine — indeed, rather than trying to “capture” customers into a bespoke system, the API actually fosters opening the systems to be freely assembled by the consumers in the way they desire. As such, making the move to business APIs is a tricky decision to make for many businesses, especially the banks.

A crowd-sourced, social media based identity system: In the current financial system, regulation impose that banks and other players conduct “Know Your Customer” (KYC) activities, with the goal of confirming the identity of people that open accounts and conduct transactions. In many occasions though, KYC proves to be very cumbersome because it implies manual checks of various documents.

Use of the open source movement in the context of financial services: Mozilla is a good example of how it is possible to create a community of millions of developers working on the same project, based on meritocracy. Outside of the well-known Android and Firefox projects, Mozilla has recently shown that open source can be applied to hardware and not only software — the \$25 Mozilla smart phone promises to be another instrument of inclusion to the internet, and also of course financial services in the long run.



Foundation for Financial Innovation:

Independent Innovation Teams: To foster the conditions in which real innovation will occur, financial services firms must create innovation teams that are independent, made up of industry outsiders, and given room to fail. This also means giving them the resources they need to try things that may fail.

Customer-Focused Innovation: Financial services firms are very transaction-focused, but they need to pivot to a customer focus when it comes to innovation. Firms must try to generate new ideas that will benefit the customer first, rather than deciding what works best for the institution and "stuffing" customer's needs into the model after the fact. Some innovations will work great in certain markets, but not others.

Networked vs. Siloed Operations: The "old" financial services business model of siloed teams and "we need to invent it here" mentality does not encourage innovation. Further, today's banks and other financial services firms have grown outward into providing more services rather than teaming with best in class providers to create a kind of innovation "grid." Financial services firms must decide what their core competencies are and create partnerships in areas where they are weaker to achieve this networked world.

Mobile/Social/Virtual World: Some of the greatest innovations down the line will likely occur in mobile payments, crowd funding/lending, virtual currencies and alternative payment systems like Paypal and Alipay.

CONCLUSION

Today the contribution of services to the economy is ever growing. Services are characterized by their intangible nature as well as the joint involvement of the producer and the consumer for the service to be enacted. This further stresses the need for an in-depth understanding of the customer's preferences. These elements can clearly be illustrated by the various financial services that can be offered to consumers and professional investors. Often legislation will even prescribe certain elements of information that need to be specified in order to collect the customer's preferences.

For the financial services industry to be truly sustainable, it needs to practice financial inclusion in embracing online technologies and mobile applications so as to be well placed to ride this emerging trend of digital banking to serve the corporate, mass affluent customers & high net worth individuals at large. This could well represent huge online opportunities for the industry as a whole.

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